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No. 95-1764-CFX Title: Saratoga Fishing Company, Petitioner
v.
J. M. Martinac & Company and Marco Seattle Inc.

Docketed: May 1, 1996 Court: United States Court of Appeals for the Ninth Circuit

Entry	Date	Proceedings and Orders
	Apr 29 1996	Petition for writ of certiorari filed. (Response due May 31, 1996)
	Jun 12 1996	DISTRIBUTED. September 30, 1996
	Aug 16 1996	Response requested.
	Sep 16 1996	Brief of respondents J.M. Martinac & Co., et al. in opposition filed.
	Sep 25 1996	REDISTRIBUTED. October 11, 1996
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	Nov 25 1996	Motion of petitioner to dispense with printing the joint appendix filed.
	Nov 27 1996	Brief amicus curiae of All Alaskan Seafoods, Inc. filed.
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	Dec 9 1996	Motion of petitioner to dispense with printing the joint appendix GRANTED.
	Dec 30 1996	Brief of respondents J.M. Martinac & Co. and Marco Seattle, Inc. filed.
	Dec 30 1996	Brief amici curiae of National Association of Manufacturers & Raychem Corporation filed.
	Jan 8 1997	CIRCULATED.
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	Feb 7 1997	Record filed.
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No. 951764

In The

Supreme Court of the United States

October Term, 1995

SARATOGA FISHING CO.,

Petitioner,

vs.

J.M. MARTINAC & CO.;
MARCO SEATTLE, INC.,

Respondents.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Does the Ninth Circuit's majority opinion on how courts are to determine "other property" in maritime product liability suits conflict with this Court's decision in *East River S.S. Corp. V. Transamerica Delaval Inc.*, 476 U.S. 858 (1986)?

2. Has the Ninth Circuit, by holding that the "product" at issue in maritime product liability suits is the ship as sold, not by the manufacturer, but by the last person who owned the ship, abrogated the well established law of maritime products liability set forth in *East River,* and the decisions of other courts, including the Fifth Circuit's opinion in *Nicor Supply Ships Associates v. General Motors,* 876 F.2d 501, 505-06 (5th Cir. 1989)?

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CORPORATE DISCLOSURE

Petitioner Saratoga Fishing Co. has no parent company or subsidiaries.

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OPINIONS BELOW

The opinion of the Ninth Circuit Court of Appeals, filed October 26, 1995 (App., 4a), is reported at 69 F.3d 1432 (9th Cir. 1995). Neither the district court's Findings on Liability (App., 114a), nor its Oral Findings on damages (App., 173a) are reported. The original opinion of the Ninth Circuit Court of Appeals, filed April 25, 1995 (App., 80a), and the first revised opinion of the Ninth Circuit Court of Appeals, filed August 4, 1995 (App., 43a) are not published.

STATEMENT OFJURISDICTION

The Ninth Circuit Court of Appeals entered its order denying rehearing of Saratoga's motion for reconsideration on January 30, 1996. App., 1a. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1). Because these claims arose on the high seas, they fall within the admiralty jurisdiction of the federal courts under 28 U.S.C. §1333.

STATEMENT OF THE CASE

Petitioner Saratoga Fishing Co. ("Saratoga") sued Respondents for damages resulting from a conflagration that occurred on board the M/V SARATOGA on or about January 16, 1986, in which M/V SARATOGA burned and sank. M/V SARATOGA was originally purchased in or about 1972 from the manufacturer, J.M. Martinac & Co. ("Martinac"), by Joseph Madruga, a private individual. The hydraulic system on the vessel was designed by Marco Seattle Inc. ("Marco"). The vessel was completed in 1972, taken to Panama and outfitted with a seine and other fishing equipment, and Madruga began fishing operations with the vessel, with Manual Vargas as its captain.

In 1974, Joseph Madruga sold M/V SARATOGA to the Manual S. Vargas, Jr. Corporation, which later changed its name to Saratoga Fishing Co. At the time of that sale, M/V SARATOGA was equipped with five speedboats, a purse skiff, a seine, and various electronic equipment. On or about January 16,1986, a hydraulic hose detached from its coupling, spraying hydraulic fluid onto the turbocharger. Because Martinanc and Marco had failed to provide any effective shielding, the hydraulic fluid sprayed onto the adjacent engine surfaces and turbocharger and ignited. The resulting conflagration burned and sank M/V SARATOGA. The crew just managed to get off the ship into a skiff before the vessel sank.

The district court concluded that Marco and Martinanc were strictly liable for the loss of M/V SARATOGA in that the hydraulic system was defectively designed. The court awarded damages to Saratoga in the amount of $452,326, approximately one-third of what it determined were the total of Saratoga's damages. The total damage award was reduced by two thirds for comparative negligence. The award included the loss of "other property" on board M/V SARATOGA, including the tuna catch, seine, skiff, fuel, equipment, payments by Saratoga to the crew for their personal property losses, the cost of rescue and certain cash. With pre-judgment interest, the total award to Saratoga after reduction by two-thirds for comparative negligence came to $734,940.38.

All parties appealed the district court's decision on various grounds, only one of which, the determination of "other property," is at issue in this Petition. In its original opinion, issued April 25, 1995 (the "Original Opinion") (App., 80a), the panel correctly recognized that the "product" in products liability cases, including maritime products liability cases, is determined by what the *manufacturer* places in the stream of commerce. The court therefore agreed with the Fifth Circuit that,

> additions to a vessel should be considered other property "separate from the product that the ***manufacturer originally*** sold, if the distinction enunciated in *East River* between a 'product' and 'other property' is to have any meaning."

App., 108a, *quoting Nicor,* 876 F.2d at 505 (emphasis added, italics in the original). To distinguish the "product" from "other property" on M/V SARATOGA, the court looked to "the vessel that Martinac sold to Madruga in 1972." App., 108a. Including the items not part of the vessel originally sold by Martinac to Madruga,

> would undermine the 'other property' exception contained in *East River.* Under that rationale, the product would envelop everything else useful in the operation of the vessel, which is not consistent with the balance struck by the Supreme Court.

App., 108a.

On August 4, 1995 (the "First Revised Opinion") (App., 43a), the same panel scuttled its well-reasoned Original Opinion and changed course 180 degrees. Misreading *East River,* the panel unanimously held that the manufacturer's "product" is defined for strict products liability as the object that was last transferred from *any* seller to a buyer, even if the seller, as in this case, is a private person and *not* a "seller . . . who is engaged in the business of selling such a product" as defined by the Restatement (Second) of Torts, Section 402(1)(a). App., 72a-72b. Saratoga then moved for reconsideration, noting that the court's ruling abandoned Section 402A of the Restatement (Second) of Torts, ignored the Ninth Circuit's earlier decision in

Pan-Alaska Fisheries, Inc., 565 F.2d 1129 (9th Cir. 1977) adopting Section 402A as the law of the Ninth Circuit, placed the Ninth Circuit in direct conflict with the Fifth Circuit by disregarding the well established maritime rule set by the Fifth Circuit in *Nicor Supply Ships Associates v. General Motors*, 876 F.2d 501 (5th Cir. 1989) and, and misread and placed the Ninth Circuit in conflict with this Court's seminal decision in *East River v. Transamerica Delaval*, 476 U.S. 858 (1986). Saratoga again sought rehearing.

On October 26, 1995, the winds shifted again and a third superseding opinion was issued (the "Second Revised Opinion"). App., 4a. It is this opinion that is at issue in this Petition. In the Second Revised Opinion, only two members of the panel, the Honorables Beezer, J. and Ezra, J. (the "majority"), voted to stand by their First Revised Opinion of August 4, 1995. The third member, the Honorable Noonan, J., parted company with the majority on its determination of "other property," recognizing that its decision placed this Circuit in conflict not only with the Fifth Circuit's decision in *Nicor*, but with the Ninth Circuit's previous decision in *Pan-Alaska* and with this Court's decision in *East River* as well. App., 40a-41a. That dissent, set forth in full, encapsulates perfectly the Ninth Circuit's error and states the principal basis for this Petition:

> I concur in the opinion of the court, except as to its exclusion of damages for the skiff, seine net, fuel, spare parts and other miscellaneous equipment sold by Madruga to Saratoga Fishing as part of the sale of the M/V SARATOGA. None of this property was manufactured or sold by Martinac. Under *East River*, 476 U.S. 858, 867 all of it was 'other property,' damages for which are recoverable in tort. The court abandons *East River* and puts this circuit in conflict with another major maritime circuit, *Nicor Supply Ships Associates v. General Motors*, 876 F.2d 501, 505-06 (5th Cir. 1989). The opinion also repudiates controlling authority in this circuit, *Pan-Alaska Fisheries, Inc. v. Marine Construction & Design Co.*, 565 F.2d 1129 (9th Cir. 1977). That case accepted 'as the law of products liability in this circuit, at least for this case arising in admiralty,' the Restatement (Second) of Torts, §402A *Id.* at 1135. Under the Restatement, the original seller of the product in a defective condition that is unreasonably dangerous that has entered the stream of commerce is strictly liable to the ultimate consumer for physical harm caused to that consumer's property. Saratoga Fishing is here the ultimate consumer; Martinac is the original seller; the property damaged was Saratoga Fishing's and no more part of the product sold by Martinac than was the tuna catch for which damages are granted.
>
> The court appears to have been swayed by the consideration that additions made by a middleman could increase the original seller's liability. That of course is a risk the seller of an unreasonably dangerous, defective product takes. If the explosion had occurred while Madruga still owned the boat after adding the skiff and net, there is no doubt that Martinac would have been liable for those additional items. Martinac's exposure should not decrease because

> Madruga sold the ship to Saratoga Fishing. Whatever theory one adopts, the liability of the original seller may change as the ultimate consumer adds or subtracts property which can be affected by the defective product. The theory of strict liability holds that the seller is stuck whatever foreseeable damage to the consumer's other property his product causes.

App., 40a-41a, Noonan, J., concurring and dissenting.

REASONS FOR GRANTING THE WRIT

I.

THE NINTH CIRCUIT'S RULING PLACES THE NINTH CIRCUIT IN DIRECT CONFLICT WITH THIS COURT'S DECISION IN *EAST RIVER* AND WITH THE FIFTH CIRCUIT'S DECISION IN *NICOR* AND OTHER CASES.

The Ninth Circuit is a major maritime law court. With all due respect to the Ninth Circuit, the justices in the majority in the October 26 Second Revised Opinion issued an opinion that will, if given effect, totally and wrongfully disrupt maritime products liability law in not only the Ninth Circuit, but in the United States as a whole. By misreading and misapplying *East River*, the Ninth Circuit has decided an important question of maritime law "in a way that conflicts with relevant decisions of this Court." Rules of the Supreme Court, Rule 10(c). Moreover, the Ninth Circuit has, if its decision is given effect, "entered a decision in conflict with the decision of another United States court of appeals on the same important matter," namely, the Fifth Circuit's ruling in *Nicor* and other decisions. Rules of the Supreme Court, Rule 10(a).

The Ninth Circuit's erroneous decision creates an intolerable situation that will effectively destroy claims for "other property" by second and subsequent purchasers of a vessel, even though the damage to other property was caused by the exact same defect that existed at the time the manufacturer sold the vessel to the first purchaser. Effectively, once a vessel is sold or transferred by the first buyer, the second vessel buyer has no remedy for product defects that cause damage to "other property" added to the vessel by the first buyer. Resales or transfers of vessels to another owner or operator are, however, commonplace, and often occur within a short time of the useful life of the vessel. It is also common that, as in this case, after a vessel is purchased, other items are added to outfit it for its particular purpose. These additional items, as can be seen in this case, can amount to as much or more than one-third of the total value of the vessel.

II.

THE NINTH CIRCUIT ERRED IN DECIDING HOW "OTHER PROPERTY" IS DETERMINED IN MARITIME PRODUCT LIABILITY CASES.

Under its Original Opinion, the panel correctly recognized that the "product" is delineated by that which a *manufacturer* places in the stream of commerce. The Original Opinion correctly held that the distinction between the "product" and "other property" in a products liability claim turned on whether the property was "'separate from the product that the ***manufacturer originally*** sold" to the first buyer; in this case, what Martinac sold to Joseph Madruga, the original buyer of M/V SARATOGA. App., 108a (emphasis added, italics in the original), *citing Nicor,* 876 F.2d at 505. The panel's Second Revised Opinion (and its First Revised Opinion) misread *East River* as holding that "product" is defined for strict products

liability as the object that was last transferred from any seller to a buyer, even if the seller, as in this case, is an occasional seller, *not* a "seller . . . who is engaged in the business of selling such a product" as defined by the Restatement (Second) of Torts, Section 402(1)(a). App., 33a-35a.

The Second Revised Opinion abrogates fundamental products liability principles that (1) only commercial sellers (*e.g.*, manufacturers and distributors), not end-users of a product can be held liable for a product's defects; (2) the "product" at issue in strict products liability analysis is the product the manufacturer or distributor placed into the stream of commerce; (3) product liability cannot be disclaimed by warranty; and (4) "[t]he consumer's cause of action does not depend upon the validity of his contract with the person from whom he acquires the product. . . ." Restatement (Second) of Torts, §402A, cmt. m (1977). The Ninth Circuit erred by deviating from first principles of product liability law, then misreading *East River* as supporting its deviation. The Ninth Circuit's error is profound and should be corrected.

III.

THE NINTH CIRCUIT MISREAD *EAST RIVER* TO IMPORT CONTRACT ANALYSIS INTO PRODUCTS LIABILITY TORT LAW.

The Ninth Circuit erroneously misread *East River* as holding that a downstream sales contract between consumers determines "the product" at issue for purposes of distinguishing "the product" from "other property." App., 33a-35a. The Ninth Circuit was wrong. Looking to a downstream contract to define a manufacturer's "product" for strict products liability purposes ignores *East River's* determination that the recovery of property damages under maritime products liability law, including strict

products liability, is controlled by Section 402A of the Restatement (Second) of Torts. *East River*, 476 U.S. at 875, *citing with approval Pan-Alaska Fisheries, Inc.*, 565 F.2d 1129, 1135 (9th Cir. 1977) (adopting Restatement (Second) of Torts Sec. 402A (1965)).

A. Strict Products Liability Law Applies Only to Sales by Commercial Manufacturers, Distributors or Retailers to Consumers.

The Ninth Circuit initially erred when it framed the question before it as "whether the 'product' changed when Madruga added various components, including a skiff, seine and other miscellaneous parts, to the vessel and resold it to Saratoga Fishing." App., 33a-34a (emphasis added). By answering "yes," the Ninth Circuit placed Joseph Madruga, a consumer, in the shoes of Martinac, the manufacturer of M/V SARATOGA, for purposes of determining what Martinac's product was. The Ninth Circuit was wrong.

Section 402A of the Restatement (Second) of Torts, cited with approval by this Court in *East River* and adopted by the Ninth Circuit in *Pan-Alaska Fisheries, Inc.*, 565 F.2d at 1134-1135, provides as follows:

> § 402 A. Special Liability of Seller of Product for Physical Harm to User or Consumer.
>
> (1) One who *sells* any product in a defective condition unreasonably dangerous *to the user or consumer or to his property* is subject to liability for physical harm thereby caused to the *ultimate* user or consumer, or to his property, if

> (a) the seller is *engaged in the business of selling such a product*, and
>
> (b) it is expected to and does reach the user or consumer without substantial change in the condition in which it is sold.

(2) The rule stated in Subsection (1) applies although

> (a) the seller has exercised all possible care in the preparation and sale of his product, and
>
> (b) *the user or consumer has not bought the product from or entered into any contractual relation with the seller.*

Restatement (Second) of Torts, § 402A (1977) (emphasis added).

A "seller" of a product under Section 402A is unequivocally not a consumer reselling the product, but a commercial seller (*e.g.*, a manufacturer, distributor) of that product:

> The rule stated in this Section applies to any person engaged in the business of selling products for use or consumption. It therefore applies to any *manufacturer* of such product, to any *wholesale or retail dealer or distributor*, and to the operator of a restaurant.

Restatement (Second) of Torts, § 402A, cmt. f (1977) (emphasis added). A "product," as defined by the most recent Tentative Draft of the Restatement (Third) is not an item resold by one consumer to another consumer but,

> something *distributed commercially* for use or consumption. Most but not necessarily all products are tangible personal property; most have been subjected to processing and fabricating prior to entering the stream of commerce; and most pass through a commercial chain of distribution before ultimate use and consumption.

Restatement (Third) of Torts: Products Liability, § 4 (Tentative Draft No. 2, March 13, 1995) (emphasis added).

Joseph Madruga indisputably was not in the business of selling tuna boats. Madruga was a small shipowner who sold his boat to his former captain. App., 6a. He was *not* a commercial seller when he sold M/V SARATOGA. He therefore could *not*, by definition, have placed Martinac's product into the stream of commerce as a seller under Section 402A of the Restatement, and he could not "change" the manufacturers' product for product liability purposes.

B. The Ninth Circuit's Second Revised Opinion Undermines the Rationale for Applying Strict Products Liability Only to Commercial Manufacturers and Distributors.

The rationale for strict products liability, fully recognized by *East River*, the Restatement, and the Ninth Circuit itself, centers on the *manufacturer's* ability to spread the risk of defects, and to correct defects in the product:

> [T]he justification for the strict liability has

been said to be that the seller, *by marketing his product for use and consumption*, has undertaken and *assumed* a *special responsibility toward* any member of *the consuming public* who may be injured by it; that the *public* has the right to and does expect, in the case of products which it needs and for which it is forced to rely upon the seller, that reputable sellers will stand behind their goods; that public policy demands that the burden of accidental injuries caused by products intended for consumption *be placed upon those who market them*, and be *treated as a cost of production* against which liability insurance can be obtained; and that the consumer of such products is entitled to the maximum of protection at the hands of someone, and the proper person to afford it are *those who market the products.*

Restatement (Second) of Torts, § 402A, cmt. c (1977) (emphasis added). This Court in *East River* likewise understood that this rationale applied to the *manufacturer*, not the occasional downstream seller:

> The *manufacturer* is liable whether or not it is negligent because 'public policy demands that responsibility be fixed wherever it will most effectively reduce the hazards to life and health inherent in defective products *that reach the market.*' *Escola v. Coca Cola Bottling Co. of Fresno*, 24 Cal.2d, at 462, 150 P.2d, at 441 (opinion concurring in judgment).

East River, 476 U.S. at 866-867 (emphasis added).

East River understood that a manufacturer's strict liability for defective products stands separate and apart from contract based warranty law and is based on a wholly separate rationale:

> Products liability grew out of a public policy judgment that people need more protection from dangerous products than is afforded by the law of warranty. *See Seely v. White Motor Co.*, 63 Cal.2d 9, 15, 45 Cal.Rptr. 17, 21, 403 P.2d 145, 149 (1965).

East River, 476 U.S. at 866.[1]

Under the Ninth Circuit's reasoning, an occasional seller like Joseph Madruga cannot be held liable under products liability law for a products' defects, and none of the rationales upon which strict product liability rests apply to him. Yet the Ninth Circuit's bizarre conclusion is that this same occasional seller can nonetheless "change" the manufacturer's "product" for products liability purposes. App., 34a-35a. The focus of the Ninth Circuit's inquiry was not on what the manufacturer placed into the stream of commerce, but what the downstream consumer, Madruga, resold. App., 34a-35a. The district court (and the dissent) correctly rejected this awkward result: "I conclude that the definition of the vessel . . . would change with each successive sale of the boat, including and then excluding the new or removed items on board. This rule of law would be awkward and illogical." App., 176a; *see also* App., 41a, Noonan, J., concurring and dissenting.

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1. Again siding with *Seely*, *East River* recognized that damage to property did not differ from damage to persons in strict products liability: "For similar reasons of safety, the *manufacturer's* duty of care was broadened to include protection against property damage. [citations omitted] Such damage is considered so akin to personal injury that the two are treated alike. *See Seely*, 63 Cal. 2d at 19, 45 Cal. Rptr., at 24, 403 P.2d, at 152." *East River*, 476 U.S. at 867.

C. The Ninth Circuit Misunderstood That in *East River*, this Court First Determined That Products Liability Law Did Not Apply Before Going on to Reach a Decision under Warranty Law.

The Ninth Circuit claimed that *East River* "focused on the terms of 'the charterers' agreements with the owners." App., 34a. The Ninth Circuit believed that "the contract being discussed" throughout *East River* was the contract "between the first buyer and the bareboat charterer, who the court treated as equivalent to a second buyer." App., 34a-35a. The Ninth Circuit was wrong. It misunderstood whom the "buyer" was that this Court was referring to in *East River* when, in the first part of its decision, this Court performed its products liability analysis to determine what precisely the "product" at issue was. Like *Shipco 2295, Inc. v. Avondale Shipyards, Inc.*, 825 F.2d 925 (5th Cir. 1987), *East River* focused on the "product" from the perspective of the first purchaser, the boat owners[2], not the bareboat charterers.[3] *East River* did not focus on the downstream

2. The owners were subsidiaries of Seatrain. The ships had been constructed under contract between these subsidiaries of Seatrain and another Seatrain subsidiary, Shipbuilding. Shipbuilding had, in turn, contracted the design and manufacture of the ships to Delaval. Finally, the bareboat charterers of the ships were also Seatrain subsidiaries. *East River*, 476 U.S. at 859-860.

3. The Ninth Circuit may well also have misapprehended the teaching of *Shipco* and its application to this case. After this Court decided in *East River* that recovery in tort was not available where a component part of a vessel injured only itself, *id.*, 476 U.S. at 871, *Shipco* faced the next question. That is, could a component part manufacturer be held liable in tort for damage to the rest of the vessel caused by the defective component part? The Fifth Circuit answered "no," at least insofar as the component part (*e.g.*, the defective steering gear) had been sold to the original purchaser as an integral part of the completed vessel. *Shipco*, 825 F.2d at 929-930. The focus of *Shipco* was identification of the final, completed product the first purchaser bought from the manufacturer. That case has no bearing where, as here, the sale was a downstream sale between two private parties.

agreement between the owners of the vessels and the "second buyers" the bareboat charterers *until after it had determined that strict products liability law did not apply.*

Thus, in the first part of its decision, *East River* held that the plaintiffs had no products liability claims because only "economic damage," that is, damage to the product itself, was at issue. *East River*, 476 U.S. at 867. It made this determination only after it had decided what "the product" at issue was. To do this, the Court looked to what had been "*supplied by Delaval*," the *manufacturer*, to the owners of the ships at the time of delivery to the owners. Because "each turbine was *supplied by Delaval* [the manufacturer] as an integrated package," each turbine was "properly regarded as a single unit." *East River*, 476 U.S. at 867. As a result, because the "defectively designed turbine components [had] damaged only the turbine itself," "*there was no damage to 'other' property.*" *East River*, 476 U.S. at 867.

Once the Court had determined that the turbines were "the product" sold by Delaval to the owners, and that the turbines had damaged only themselves, the Court considered whether damage caused by the product to itself was recoverable in tort under a products liability theory. The Court examined the dispute between those courts that held that damage to the product itself was recoverable, and those that did not. *East River*, 476 U.S. at 868-871. Ultimately, the Court sided with California's Supreme Court decision in *Seely*, and held that damage to the product itself, in that case the turbine supplied by Delaval, was "economic damage" that could not be recovered in tort under a products liability theory. Therefore, such damage could not be recovered in tort by *either* the owners or the bareboat charterers. *East River*, 476 U.S. at 867, 875. Products liability law was simply the wrong instrument. The Court therefore proceeded to its analysis under warranty law.

D. The Ninth Circuit Confused *East River*'s Discussion of Warranty Law with its Discussion of Products Liability Law.

Because it did not distinguish between *East River's* discussion of products liability law and its discussion of warranty law, the Ninth Circuit erroneously imported this Court's discussion of warranty law into its analysis of Saratoga's product liability claims. The Ninth Circuit thus misunderstood this Court's discussion of "the benefit of the bargain" under warranty law. Its error is seen in the phrasing of its question:

> We must decide whether the "product" changed when Madruga added various components, including a skiff, seine and other miscellaneous parts, to the vessel and resold it to Saratoga Fishing.
>
> We are guided by the policies set forth in *East River*, where the Court stated that *the focus of the product* should be on the failure of the purchaser to receive the *benefit of its bargain.* Warranty and contract law are appropriate for this type of situation. Here, the purchaser is Saratoga Fishing and the object of its bargain was the M/V SARATOGA with the components already installed. Saratoga Fishing purchased the vessel "as is." Madruga made no "warranty or representation of vessel condition."

App., 34a (emphasis added).

The Ninth Circuit missed this Court's point. The "benefit of the bargain" and "as is" language in *East River* relied on by the Ninth Circuit, App., 34a, played no part in *East River's* products

liability analysis, but was only relevant to determine whether the charterers had any remedy in warranty. This analysis came only after this Court had decided that products liability law did not apply because the product, the turbines, had only injured themselves. *East River,* 476 U.S. at 867. This Court found that the bareboat charterers did not have any remedy *in warranty.* No warranties were available because there were no warranties given by the *owners* to the bareboat charterers. This Court took the parties at their word that the charterers did not have standing to sue on the manufacturer's warranties to the owners because those warranties had not been transferred to the bareboat charterers by the owners. *East River*, 476 U.S. at 875. At this point, this Court determined that, under contract law, there was "no reason to extricate the parties from their bargain." *East River,* 476 U.S. at 875. None of this discussion, contrary to the Ninth Circuit's reading, had *anything* to do with this Court's products liability analysis in *East River.*

E. *East River* Understood That "Economic Loss" Did Not Include Damage to Property Physically Separate From the Defective Product.

The Ninth Circuit misunderstood what *East River* meant by "economic loss" in the context of products liability law, and its relationship to "benefit of the bargain" under warranty law. App., 33a-34a. Agreeing with the California Supreme Court's decision in *Seely*, this Court understood "economic" damage to mean damages proximately caused when a product fails to perform as the purchaser expected:

> [S]ince by definition no person or other property is damaged, the resulting loss is purely economic. Even when the harm to the product itself occurs through an abrupt, accident-like event, *the resulting loss due to*

> *repair costs, decreased value, and lost profits* is essentially the failure of the purchaser to receive the benefit of its bargain—traditionally the core concern of contract law. See E. Farnsworth, Contracts Sec. 12.8, pp. 839-840 (1982).

East River, 476 U.S. at 870 (emphasis added).

Because it failed to distinguish this Court's discussion of product liability law from its discussion of warranty law in *East River*, the Ninth Circuit misapprehended *East River's* "benefit of the bargain" language as applying to damages caused by a defective product to other physically distinct property, regardless of whether the damaged property was manufactured, assembled and sold as a single finished product by the same seller. App., 34a-35a. The Ninth Circuit was wrong. "Economic loss" analysis focuses not on the damage to persons or property extrinsic to the product placed on the market by the manufacturer, but on unlimited expectation damages that could be proximately caused by a complex, defective product made up of several components that failed to perform the work expected. *East River*, 476 U.S. at 872-873. Allowing tort recovery against a Section 402A seller in situations where the complex product it sold damages only itself would, as *Seely* explained, swallow up the price/limitation-of-damages tradeoff allowed by warranty law. *East River* agreed with this assessment. *Id.*, 476 U.S. at 873 ("The manufacturer can restrict its liability, within limits, by disclaiming warranties or limiting remedies. *See* U.C.C. §§ 2-316, 2-719. In exchange, the purchaser pays less for the product.") The Court recognized the "need to keep products liability and contract law in separate spheres," *id.*, 476 U.S. at 870-871, and accordingly performed its products liability analysis independent of its warranty law analysis:

> Products liability grew out of a public policy judgment that people need more protection from dangerous products than is afforded by the law of warranty. See Seely v. White Motor Co., 63 Cal.2d 9, 15, 45 Cal.Rptr. 17, 21, 403 P.2d 145, 149 (1965). It is clear, however, that if this development were allowed to progress too far, contract law would drown in a sea of tort. See G. Gilmore, The Death of Contract 87-94 (1974). We must determine whether a commercial product injuring itself is the kind of harm against which public policy requires manufacturers to protect, *independent of any contractual obligation.*

East River, 476 U.S. at 866 (emphasis added).

Seely explained that warranty law could *not* shield a manufacturer from liability for defects in its product that create an "unreasonable risk of harm" to persons or property physically distinct from its product:

> The distinction that the law has drawn between tort recovery for physical injuries and warranty recovery for economic loss is not arbitrary and does not rest on the 'luck' of one plaintiff in having an accident causing physical injury. The distinction rests, rather, on an understanding of the nature of the responsibility a manufacturer must undertake in distributing his products. *He can appropriately be held liable for physical injuries caused by defects by requiring his goods to match a standard of safety defined in*

> *terms of conditions that create unreasonable risks of harm. He cannot be held for the level of performance of his products in the consumer's business unless he agrees that the product was designed to meet the consumer's demands.* A consumer should not be charged at the will of the manufacturer with bearing the risk of physical injury when he buys a product on the market. He can, however, be fairly charged with the risk that the product will not match his economic expectations unless the manufacturer agrees that it will.

Seely, 63 Cal. 2d at 18 (emphasis added). *East River* understood and agreed with the *Seely* analysis. *East River*, 476 U.S. at 871-872.

The price/limitation-of-commercial damages balance that is the "benefit of the bargain" between the manufacturer and the original purchaser under warranty law has no application where, as here, the product placed into the stream of commerce by a manufacturer results in harm to persons or property physically distinct from the product sold by the manufacturer. Contrary to the Ninth Circuit's reading, nothing in East River is "inconsistent" with holding a product manufacturer fully liable in tort for damages caused by its product to persons and property physically distinct from the product. App., 35a.

IV.

THE NINTH CIRCUIT'S DECISION PLACES IT IN DIRECT CONFLICT WITH THIS COURT, THE RESTATEMENT SECOND AND THE FIFTH CIRCUIT, WHICH LOOK TO WHAT THE 402A SELLER DELIVERED, NOT TO WHAT A DOWNSTREAM CONSUMER SOLD, TO DETERMINE THE "PRODUCT" SOLD BY THE 402A SELLER.

Except for the Ninth Circuit (if the Ninth Circuit's revised decision stands), the unanimous rule is that if a defective product proximately causes damages to a person's property that is physically distinct from the defective product, the injured party is entitled to tort damages against the 402A seller of the defective product. That physically distinct property will be treated as "other property" for *East River* damage limitation purposes. This rule is logical and true even if both the defective product and the damaged property came to the injured owner by way of a transaction involving a non-402A seller as in this case and as in *Nicor*. Hence, as the Fifth Circuit held in *Nicor*, "the finished vessel delivered by the *manufacturer to the purchaser* is the product — the object of the contract...." *Nicor*, 876 F.2d at 505 (emphasis added).[4]

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4. This determination is also made explicit in the Tentative Draft of the Restatement (Third) of Torts, which specifically defines and discusses "economic loss" to property, finding "other property" to be property "exclusive of the product itself":

> § 6. Definition of "Harm to Persons or Property": Economic Loss
>
> For purposes of this Restatement the term "harm to persons or property" includes economic loss only when caused by harm to:

(Cont'd)

No court other than the Ninth Circuit has ever held that a downstream sales contract between two consumers determines the boundaries of what a manufacturer's "product" is for purposes of defining "other property." Numerous cases, on the other hand, clearly focus on the product placed on the market by the manufacturer. In *Nicor*, the court looked to the "the object of the contract" between the shipbuilder and the plaintiff buyer to determine that equipment placed on the vessel by the plaintiff was "other property." *Nicor*, 876 F.2d at 505. Likewise, in *Shipco*, 825 F.2d 925, the court denied recovery under *East River* against a manufacturer of a component part of a ship for economic damages caused by the part to the rest of the ship,

(Cont'd)

> (a) the plaintiff's person;
>
> (b) the person of another when harm to the other interferes with a legally protected interest of the plaintiff;
>
> (c) *the plaintiff's property other than the defective product itself.*

Restatement (Third) of Torts: Products Liability, § 6 (Tentative Draft No. 2, March 13, 1995) (emphasis added).

The Third Restatement then defines "other property":

> *'Other property,' in its most basic sense, may be defined as tangible items belonging to the product purchaser, exclusive of the product itself.* Numerous cases hold that where damage is done by a defective product to any tangible item which is *physically distinct* from it, the damage to the 'other property' may be recoverable in tort.

Restatement (Third) of Torts: Products Liability, § 6, cmt d at 189 (Tentative Draft No. 2, March 13, 1995) (emphasis added).

where the component was sold by the shipbuilder to the first purchaser as original equipment; that is, it was part of the complete ship sold by the manufacturer to the first consumer/purchaser.[5]

In *McDermott, Inc. v. Clyde Iron*, 979 F.2d 1068 (5th Cir. 1993), the court specifically stated how it determined the identity of "the product," and therefore, "other property": "The object of the [purchaser]-[manufacturer] contract was the manufacture, design, and sale of the crane *and that is the relevant inquiry.*" *McDermott*, 979 F.2d at 1077-1078 (emphasis added). *See also Mays Towing v. Universal Machinery Co.*, 755 F. Supp. 830 (S.D. IN. 1990) (damage to new engines placed in vessel were covered by warranty law; but damage to vessel caused by the defective engines was recoverable as "other property" under products liability law.)

5. In *Shipco* the court recognized that the question before it was, "what is the product?" *Id.*, 825 F.2d at 928. To answer this question, it asked,

> what is the object of the contract or bargain that governs the rights of the parties? The completed vessels were obviously the objects of the contract. Shipco (footnote omitted) did not bargain separately for individual components of each vessel. We are persuaded that those same vessels that were the object of the contract must be considered "the product" rather than the individual components that make up the vessels.

Id., 825 F.2d at 928. The point was that "Avondale (the manufacturer) sold the completed vessels to Shipco." *Id.*, 825 F.2d at 929. *Shipco's* analysis was the equivalent of asking, "what did General Motors sell the consumer of a new Oldsmobile?" That case had absolutely nothing to do with the subsequent question, which the Ninth Circuit answered incorrectly, "if the first consumer sells the Oldsmobile to a second consumer a few years later, do the box of toys in the trunk, the child seat and the tool box the first owner sold with it become part of GM's "product" for product liability purposes?

It is undisputed that the skiff, net, fuel, spare parts, speed boats and miscellaneous equipment added to M/V SARATOGA by Madruga and sold to Saratoga were *not* sold by Respondents at any time and are physically distinct individual products in their own right sold by other manufacturers after Martinac and Marco sold the boat to Madruga. App., 6a. Under fundamental products liability law, because Martinac and Marco did not place these items into the stream of commerce, they cannot be considered Respondents' "product" for purposes of strict products liability. They are then, by definition, "other property" recoverable by Saratoga.

V.

THE NINTH CIRCUIT'S RULING CREATES ANOMALIES IN THE LAW.

The Ninth Circuit opinion will create chaos in maritime law if given effect. For example, if a first purchaser keeps a vessel for 20 years, adding many pieces of equipment to the ship during that period, the manufacturer clearly can be held liable in tort should this "other property" be damaged or destroyed by a defect in the ship. Thus, the manufacturer's liability would increase every time the vessel is modified, so long as it is owned by the first purchaser. Yet if the first purchaser sells the ship and all its additions to purchaser two after owning it for 20 years and one day, the manufacturer's liability for the "other property" *immediately* springs back to zero. As a result, the manufacturer's liability for precisely the same damage caused by precisely the same defect would turn on whether, by luck, the ship was sold the day before the defect manifested itself. *See* App., 41a, Noonan, J., concurring and dissenting.[6]

6. The district court also rejected this outcome as irrational. App., 176a.

Even more troublesome would be the suit in which a vessel manufacturer is sued for a personal injury caused by a defective piece of "other property" (*e.g.*, a skiff) that the manufacturer did not sell with the vessel. The plaintiffs would claim, under the Ninth Circuit's reasoning, that the defective "other property" became part of the manufacturer's "product" when the vessel was sold to a second buyer. The manufacturer could be held liable for damages caused them by this "other property."

Similarly, the manufacturer of a skiff that, because of a defective steering mechanism, when released turns and collides with the vessel from which it was released, will claim that it cannot be held liable for damage to the ship because the skiff became part of the vessel manufacturer's "product" when the vessel, with the skiff, was sold to a second buyer.[7] Therefore, the defense will contend, the "product" only injured itself, and because the skiff manufacturer did not provide the buyer with a warranty for such "economic damage," it cannot be held liable for the damage to the vessel. Similarly, because the vessel manufacturer did not provide a warranty for the skiff (after all, it was not even part of the vessel when it was sold), it too will have no liability for the damage.

7. This result would, of course, go far past *Shipco*, which decided only that the manufacturer of the steering mechanism that was part of the vessel when it was originally sold to the first purchaser by the manufacturer, could not be held liable for damages that mechanism caused to other parts of the vessel. *Shipco*, 825 F.2d at 930-931. In the example above, under the Ninth Circuit's reasoning, the subsequently added equipment would become part of the manufacturer's "product," for which the manufacturer presumably could be sued. App., 34a-35a.

CONCLUSION

The Ninth Circuit's Second Revised Opinion undermines and eviscerates fundamental tenets of products liability law. It places the Ninth Circuit in direct conflict with this Court's decision in *East River* and decisions of the Fifth Circuit. It places the Ninth Circuit in direct conflict with Section 402A of the Restatement (Second) of Torts. Only this Court now has the power to restore the uniformity and balance in maritime product liability law envisioned and required by *East River.* Saratoga respectfully requests that this Court grant its petition for a writ of certiorari.

Dated: April 29, 1996

Respectfully submitted,

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APPENDIX A — NINTH CIRCUIT COURT OF APPEALS ORDER DENYING PETITION FOR REHEARING FILED JANUARY 30, 1996

NOT FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 93-56344
D.C. No. CV-87-01691-JMF

SARATOGA FISHING CO.,

Plaintiff-Appellee,

v.

MARCO SEATTLE INC.,

Defendant-Appellant,

and

J.M. MARTINAC & CO.; CATERPILLAR TRACTOR CO.; SOUTHWEST MARINE HARDWARE, INC.,

Defendants.

No. 93-56368
D.C. No. CV-87-01691-JMF

SARATOGA FISHING CO.,

Plaintiff-Appellant,

v.

Appendix A

MARCO SEATTLE INC.; SOUTHWEST MARINE HARDWARE, INC.; CATERPILLAR TRACTOR CO.; J.M. MARTINAC & CO.,

Defendants-Appellees.

No. 93-56501
D.C. No. CV-87-01691-JMF

SARATOGA FISHING CO.,

Plaintiff-Appellee,

v.

J.M. MARTINAC & CO.,

Defendant-Appellant.

ORDER

Before: BEEZER and NOONAN, Circuit Judges, and EZRA, District Judge.*

A majority of the panel has voted to deny Saratoga Fishing Co.'s petition for rehearing filed November 16, 1995. Judge Beezer votes to reject the suggestion for rehearing en banc and Judge Ezra so recommends. Judge Noonan would grant the petition for rehearing and accept the suggestion for rehearing en banc.

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* The Honorable David Alan Ezra, United States District Judge for the District of Hawaii, sitting by designation.

Appendix A

The full court has been advised of the suggestion for rehearing en banc and no judge in active service has requested a vote to rehear the matter en banc. Fed. R. App. P. 35.

The petition for rehearing is DENIED and the suggestion for rehearing en banc is REJECTED.

APPENDIX B — NINTH CIRCUIT COURT OF APPEALS ORDER AND OPINION AFFIRMING IN PART, REVERSING IN PART, AND REMANDING THE MATTER TO THE DISTRICT COURT FILED OCTOBER 26, 1995

FOR PUBLICATION

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

SARATOGA FISHING CO., *Plaintiff-Appellee,* v. MARCO SEATTLE INC., *Defendant-Appellant,* and J.M. MARTINAC & CO.; CATERPILLAR TRACTOR CO.; SOUTHWEST MARINE HARDWARE, INC., *Defendants.*	No. 93-56344 D.C. No. CV-87-01691-JMF
SARATOGA FISHING CO., *Plaintiff-Appellant,* v. MARCO SEATTLE INC.; SOUTHWEST MARINE HARDWARE, INC.; CATERPILLAR TRACTOR CO.; J.M. MARTINAC & CO., *Defendants-Appellees.*	No. 93-56368 D.C. No. CV-87-01691-JMF

Appendix B

SARATOGA FISHING CO., *Plaintiff-Appellee,* v. J.M. MARTINAC & CO., *Defendant-Appellant.*	No. 93-56501 D.C. No. CV-87-01691-JMF ORDER AND OPINION

Appeals from the United States District Court
for the Southern District of California
James M. Fitzgerald, Chief Judge, Presiding

Argued and Submitted
February 8, 1995—Pasadena, California

Filed April 25, 1995
Withdrawn August 4, 1995
Filed August 4, 1995
Withdrawn October 26, 1995
Filed October 26, 1995

Before: Robert R. Beezer and John T. Noonan, Jr., Circuit Judges, and David Alan Ezra, District Judge.*

Opinion by Judge Beezer; Parital Concurrence and Partial Dissent by Judge Noonan

SUMMARY

Admiralty and Marine/Torts/Products Liability

*The Honorable David Alan Ezra, United States District Judge for the District of Hawaii, sitting by designation.

Appendix B

The court of appeals affirmed in part a district court judgment, reversed in part, and remanded. The court held that the district court correctly applied the "risk-utility" test in a design defect product liability action against a shipbuilder and the designer of the vessel's hydraulic system.

The fishing vessel M/V SARATOGA was designed and built by appellant J.M. Martinac & Co. for Joseph Madruga. During the construction process, Martinac contracted with appellant Marco Seattle Inc. to design a hydraulic system. The system was installed by Martinac and inspected by Marco.

The vessel's captain, Manuel Vargas, took the vessel to Panama, where the vessel was outfitted with a seine and other fishing equipment. The vessel then commenced tuna fishing operations. The vessel was purchased from Madruga by appellee Saratoga Fishing Co. As captain, Vargas ordered a series of modifications to various machinery and equipment: the size of the seine was increased; a larger boom and power block were installed; larger cartridges were installed in the pumps; and a 100-horsepower electric drive and pump were installed to increase power to the hydraulic system.

The Chief Engineer noticed that the hydraulic system was experiencing failures, but Vargas continued to seek increased power to the hydraulic system. An Assistant Engineer observed worn out pump cartridges and an overloaded hydraulic system. A new Chief Engineer noticed more problems with the hydraulic system. Repair work was completed in Panama. The Chief Engineer later observed a hydraulic hose seeping hydraulic fluid, but Vargas did not shut down the hydraulic system. A hydraulic hose pulled out of its coupling and hydraulic fluid sprayed up and fell back onto the hot surface of the turbocharger. The fluid ignited, and a fire spread throughout the vessel. The SARATOGA sank.

Appendix B

Saratoga Fishing brought suit in the district court against Martinac and Marco within the court's admiralty jurisdiction seeking recovery for property losses. Saratoga Fishing argued that the hydraulic system was defectively designed, and sought recovery under theories of strict liability, negligence and failure to warn. Saratoga Fishing offered the expert testimony of a naval architect, who testified that the Marco hydraulic drive system incorporated an unsafe design. In the architect's opinion, the hydraulic hoses were located too close to the hot surfaces of the engine and turbocharger. The architect noted that hydraulic hoses and couplings are prone to failure for a variety of reasons, and that the designer of the hydraulic system should have taken preventive measures such as relocating the hoses elsewhere, installing an electric instead of a diesel motor to reduce the risk of a fire developing from leaking hydraulic fluid, or isolating the hoses from the engine and turbocharger by the use of shielding.

Marco and Martinac argued that the vessel's design was not defective, that Saratoga Fishing failed to maintain the fire suppression system or the hydraulic hoses, and that Saratoga Fishing had substantially altered and misused the hydraulic system. A marine architect testified that the hydraulic system on board the vessel met well-established marine practice, and that, in his opinion, the system was not operating properly because of the modifications made by Saratoga Fishing.

The district court concluded that Marco and Martinac were strictly liable for the loss of the SARATOGA. The court found that the hydraulic system was defectively designed despite the fact that it met established marine practices, and that the placement of the hydraulic hoses in close proximity to the engine and turbocharger presented a known serious risk of fire. The court found that feasible design changes, such as the placement of a shield to isolate the hydraulic hoses from

the engine and turbocharger, would have reduced the risk. The court found that the modifications made by Saratoga Fishing did not alter the chain of causation because they did not affect the design. The court applied the "risk-utility" test, examining the risk and utility of the design along with the feasibility of alternative designs.

The district court found, however, that Saratoga Fishing was at fault due to its poor maintenance of the hydraulic system, its overuse of the system, and its failure to recognize the signs of imminent failure of the system. Saratoga Fishing's comparative fault reduced its recovery by two-thirds. The award of damages to Saratoga Fishing included losses of the tuna catch, seine, skiff, fuel, equipment, the crews' personal losses, the cost of the rescue, and Vargas' cash. The award did not include the loss of any replacement parts that Saratoga Fishing installed on the vessel or the loss of the vessel's hull. The court awarded prejudgment interest and additional interest to Saratoga Fishing until the date of the final judgment. Marco and Martinac appealed.

[1] The law of products liability, including strict liability, is recognized as part of general maritime law. [2] The Ninth Circuit has held a commercial seller of a maritime product strictly liable under Restatement (Second) of Torts § 402A in a factually similar case involving a presumably sophisticated commercial buyer. [3] In addition, a plaintiff's misuse or alteration of a product does not relate to whether the manufacturer or seller had a duty to the consumer or user. [4] The alterations made to the hydraulic system by Saratoga Fishing did not substantially alter the design of the system.

[5] In regard to the determination of whether the product was defectively designed, the language of § 402A neither compelled nor precluded the application of either the risk-

utility test or the "consumer expectations" test. [6] The district court was correct regarding the appropriateness of applying the risk-utility test in this case. If the consumer expectations test had been applied, the danger posed by the placement of the hoses of the hydraulic system in close proximity to the hot engine and turbocharger surfaces would likely have been deemed open and obvious. The risk-utility test provided a superior yardstick of whether the product was unreasonably dangerous or defective. [7] A focus on the design's benefits, risks, and feasible alternatives was a better approach to examining an alleged design defect. [8] However, the approval of an application of the risk-utility test in this case did not necessarily preclude future admiralty plaintiffs from showing a design defect using the consumer expectations test.

[9] The district court examined the risk from the design of the hydraulic system and found it to be extremely high. [10] The district court did not rely on the mere technical possibility of a safer design. [11] Due deference had to be given to the district court's consideration of the experts' testimony. Thus, the district court correctly applied the risk-utility test in finding the design of the hydraulic system defective.

[12] The district court did not find that Saratoga Fishing's misuse and alteration of the hydraulic system amounted to a superseding cause of the accident. [13] The alterations in the hydraulic system did not alter the design to the point where they superseded the design as a proximate cause of the fire.

[14] The poor maintenance of the hydraulic system, the modifications to the system, and the use of the system known to have a defective hose all contributed to the fire that caused the sinking of the vessel. Thus, the apportionment of two-thirds liability to Saratoga Fishing was not disturbed.

[15] A cause of action for damages in a products liability claim in admiralty is available only for injury to persons or "other property." [16] The "product" in this case was the vessel that was delivered to Saratoga Fishing. Because it included the skiff, net, fuel, spare parts, and miscellaneous equipment, those items were part of the product and were not recoverable in a tort action as "other property." [17] The tuna catch was not an economic loss; it was a loss of other property. Thus, the district court did not abuse its discretion in awarding damages for the tuna catch. [18] Because a product may have any number of components replaced with spare parts in the ordinary course of events, viewing such parts as "other property" would lead to absurd results. [19] Permitting recovery from Marco for the vessel's hull would undermine relevant policy.

[20] There was insufficient reason to disturb the district court's award of prejudgment interest.

Circuit Judge Noonan concurred and dissented, concurring in the majority's opinion, except as to its exclusion of damages for the skiff, seine net, fuel, spare parts, and other miscellaneous equipment sold by Madruga to Saratoga Fishing as part of the sale of the vessel.

COUNSEL

Daniel B. MacLeod, Alford & MacLeod, San Diego, California, for defendant-appellant-cross-appellee Marco Seattle, Inc.

Duncan B. Koler, Walton, Ottesen, Meads & Koler, San Diego, California, for defendant-appellant-cross-appellee J.M. Martinac & Company.

Keith Zakarin, Pillsbury, Madison & Sutro, San Diego, California, for plaintiff-appellee-cross-appellant Saratoga Fishing Company.

ORDER

The opinion filed August 4, 1995, appearing at 63 F.3d 792 (1995), is hereby withdrawn.

OPINION

BEEZER, Circuit Judge:

This products liability action in admiralty arose following an engine room fire that caused the flooding and sinking of the fishing vessel M/V SARATOGA. The district court concluded that J.M. Martinac & Company ("Martinac"), the shipbuilder, and Marco Seattle, Inc. ("Marco"), the designer of the vessel's hydraulic system, were strictly liable to Saratoga Fishing Company ("Saratoga Fishing"), the vessel owner, for damages to "other property" on the vessel because the fire and subsequent loss resulted from a defectively designed hydraulic system. The district court reduced the damages award by two-thirds, however, because of Saratoga Fishing's comparative fault in maintaining and operating that system. Both sides appeal the district court's determinations on liability and damages.[1]

We have jurisdiction over these timely appeals pursuant to 28 U.S.C. § 1291. Because we agree with all but one facet of the district court's resolution of this action, we affirm in part, reverse in part and remand.

[1]Two other defendants, Caterpillar Tractor Company and Southwest Marine Hardware, Inc., are not parties to this appeal.

Appendix B

I

We retrace the fateful path of the fishing vessel M/V SARATOGA ("SARATOGA"). The vessel was designed and built in 1971 by Martinac in its Tacoma, Washington shipyards for Joseph Madruga. During the construction process, Martinac, after consulting with Madruga, contracted with Marco to design a hydraulic system. The system was installed by Martinac and inspected by Marco.

The SARATOGA's hydraulic system included pumps, pump drives, control valves, hoses and pressure gauges all connected to a 190-horsepower Caterpillar D333 engine and turbocharger. The system operated machinery and equipment such as a power block, a boom and winches, which were necessary to use the seine (net) for tuna fishing operations. Hydraulic fluid was pumped through the system to operate the deck machinery. The fluid exited the pumps through five rubber hoses attached to the pump drive by metal couplings. The hoses rose vertically from the pump to the overhead, passing near the engine and turbocharger.

The completed vessel was launched in 1972. Its captain, Manuel Vargas, took the vessel from San Diego, where it had undergone various sea trials, to Panama where she was outfitted with a seine and other fishing equipment. The SARATOGA then commenced tuna fishing operations.

In 1974, the Manuel S. Vargas, Jr. Corporation, which was principally owned by Vargas and later changed its name to Saratoga Fishing, purchased the SARATOGA from Madruga. At the time of sale, the vessel was equipped with five speedboats, a purse skiff, a seine, and various electronic equipment. Vargas continued to serve as captain until 1979.

Appendix B

When Vargas returned to the SARATOGA as captain in 1984, the condition of the vessel had deteriorated. While overseeing a refurbishing of the vessel, Vargas ordered a series of modifications to various machinery and equipment: the size of the seine was increased; a larger boom was installed; a larger power block was installed; larger cartridges were installed in the pumps; and a 100-horsepower electric drive and pump were installed to increase power to the hydraulic system above that of the original equipment.

A new Chief Engineer joined the vessel in 1984. Wesley Ogilvie noticed on his first fishing trip that the hydraulic system was experiencing failures, such as leaking valves and breaking hoses. Nevertheless, Captain Vargas continued to seek increased power to the hydraulic system to quicken the speed at which the seine could be pursed. Assistant Engineer Lewis Jorge joined the crew in 1985, and observed worn out pump cartridges and an overloaded hydraulic system. In late 1985, Ogilvie was replaced as Chief Engineer by Mark Nielson, who noticed more problems with the hydraulic system. Hydraulic hoses needed replacement, winches were leaking hydraulic fluid, and the temperature of the hydraulic fluid was abnormally high.

Various repair work was completed on the SARATOGA when she docked in Panama late in 1985, including the replacement of seals in the hydraulic system and pump cartridges. Workers also repaired damage to the turbocharger on the main engine. On January 8, 1986, the SARATOGA departed Panama to fish for tuna near the Galiapagos Islands in the Pacific Ocean.

On the afternoon of January 16, Chief Engineer Nielson observed one hydraulic hose seeping hydraulic fluid at the coupling attaching the hose to the pump. Although Captain Vargas arranged to rendezvous with another vessel to obtain a necessary tool to manufacture a replacement hose, Vargas did not shut down the hydraulic system. Instead, Vargas utilized the system to catch more tuna late that afternoon.

A short time later, Lewis Jorge entered the engine room and observed that a hydraulic hose was "pulsating." As Jorge watched, the hose pulled out of its coupling and hydraulic fluid sprayed up from the coupling and fell back onto the hot surface of the turbocharger. The fluid ignited causing an immediate conflagration in the engine room. Jorge and Nielson attempted to extinguish the fire, but their efforts were unsuccessful.

The fire quickly spread throughout the SARATOGA, and Captain Vargas ordered the crew to abandon ship. The crew left in a skiff, and were soon rescued by another vessel. No crew member suffered serious injury. Unfortunately, the SARATOGA sank.[2]

Property losses included, in addition to the loss of the vessel, all of the fishing equipment, fuel, a substantial tuna catch stored in the vessel, crew members' personal property losses, and $16,000 in cash that Captain Vargas had placed in the vessel's safe.

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[2]Although the district court found that the cause of the SARATOGA's sinking was the flooding that occurred as a consequence of the fire, it was unable to determine exactly how and why the flooding occurred. The district court determined that resolving that question was not necessary to its disposition. We agree.

Saratoga Fishing brought the instant lawsuit in district court against Martinac and Marco within the court's admiralty jurisdiction seeking recovery for property losses. *See* 28 U.S.C. § 1333. The court conducted a 14-day trial in which it heard testimony from a variety of expert witnesses and considered a substantial amount of evidence.

At trial, Saratoga Fishing argued that the hydraulic system was defectively designed. It sought recovery under theories of strict liability, negligence, and failure to warn.

Saratoga Fishing offered, among other witnesses, the expert testimony of David Saveker, a naval architect. Saveker testified that the Marco hydraulic drive system incorporated an unsafe design. The hydraulic hoses were, in Saveker's opinion, located too close to the hot surfaces of the engine and turbocharger. As hydraulic hoses and couplings are prone to fail for a variety of reasons, Saveker noted, the designer of the hydraulic system should have taken preventive measures such as relocating the hoses elsewhere, installing an electric instead of a diesel motor to reduce the risk of a fire developing from leaking hydraulic fluid, or isolating the hoses from the engine and turbocharger by the use of shielding. Such shielding would have "screen[ed] out a large percentage of the probability of an immediate torch" from the leaking hydraulic fluid. Saveker testified that the system was "a bad accident waiting to happen."

Marco and Martinac argued that the vessel's design was not defective, that Saratoga Fishing had failed to maintain the fire suppression system or the hydraulic hoses, and that Saratoga Fishing had substantially altered and misused the hydraulic system.

Larry Grief, a marine architect, testified as an expert wit-

ness for Marco and Martinac. He stated that the hydraulic system on board the SARATOGA met well-established marine practice and was similar to those on almost every vessel he had been aboard. The hydraulic hoses, Grief noted, were designed with a safety margin of 6 to 1 over standard operating pressures. In Grief's opinion, the hydraulic system was not operating properly because of the modifications made by Saratoga Fishing. The addition of a 100-horsepower electric drive caused the hydraulic fluid to pass through the system at a higher velocity, leading to a corresponding increase in the temperature of the hydraulic fluid, which in turn caused rapid deterioration. Furthermore, the larger equipment (seine, boom, and power block) installed by Saratoga Fishing required more hydraulic power, but the installation was not accompanied by any modifications in the hydraulic hoses.

The district court concluded that Marco and Martinac were strictly liable for the loss of the SARATOGA. The court found that the hydraulic system was defectively designed despite the fact that it met established marine practices. The placement of the hydraulic hoses in close proximity to the engine and turbocharger presented a known serious risk of fire and, the district court found, feasible design changes, such as the placement of a shield or barrier to isolate the hydraulic hoses from the engine and turbocharger, would have reduced the risk. The modifications made by Saratoga Fishing did not alter the chain of causation because they did not affect the design.

The court also found, however, that Saratoga Fishing was at fault due to its poor maintenance of the hydraulic system, its overuse of the system, and its failure to recognize the signs of imminent failure of the system. Saratoga Fishing's comparative fault reduced its recovery by two-thirds.

In a later ruling, the district court awarded damages to Saratoga Fishing in the amount of $452,326, one-third of the sum it determined to be Saratoga Fishing's total damages. The award included losses of the tuna catch, seine, skiff, fuel, equipment, the crews' personal losses, the cost of the rescue, and Captain Vargas' cash.

Not included in the award was the loss of any replacement parts that Saratoga Fishing installed on the vessel. The award also did not include the loss of the vessel's hull, which the trial court had decided pretrial was not recoverable from either defendant in an admiralty products liability action.

The court awarded prejudgment interest, which raised the total award to Saratoga Fishing to $734,940.38. Finally, the court awarded additional interest to Saratoga Fishing until the date of the final judgment at the rate of $153.09 per day.

II

We review the admiralty trial court's findings of fact for clear error, and its conclusions of law *de novo*. *Havens v. F/T Polar Mist*, 996 F.2d 215, 217 (9th Cir. 1993). The existence and extent of a duty are questions of law reviewed *de novo*, while proximate cause and whether such a duty has been breached are questions of fact reviewed for clear error. *Martinez v. Korea Shipping Corp.*, 903 F.2d 606, 609 (9th Cir. 1990).

We review *de novo* the legal conclusion that damages are available. *United States v. Timberland Paving & Constr. Co.*, 745 F.2d 595, 599 (9th Cir. 1984) ("[w]e review questions of law de novo"). Finally, we review for clear error a trial court's factual findings in support of an award for damages. *Bergen v. F/V St. Patrick*, 816 F.2d 1345, 1347 (9th Cir. 1987), *cert. denied*, 493 U.S. 871 (1989).

III

[1] Saratoga's claims fall within the admiralty jurisdiction, as they arose on the high seas. 28 U.S.C. § 1333; *see Jerome B. Grubart, Inc. v. Great Lakes Dredge & Dock Co.*, 115 S. Ct. 1043, 1047 (1995). We apply, as the district court did, substantive admiralty law, which, absent a federal statute, is the general maritime law. *East River S.S. Corp. v. Transamerica Delaval Inc.*, 476 U.S. 858, 864 (1986). The law of products liability, including strict liability, is recognized as part of the general maritime law. *Id.* at 865; *Pan-Alaska Fisheries, Inc. v. Marine Constr. & Design Co.*, 565 F.2d 1129, 1135 (9th Cir. 1977).

In holding that a strict products liability action would lie in admiralty, we adopted the Restatement (Second) of Torts § 402A (1965) as "the law of products liability in this circuit" because it was "the best and most widely-accepted expression of the theory of strict products liability." *Pan-Alaska*, 565 F.2d at 1135. Section 402A provides as follows:

> (1) One who sells any product in a defective condition unreasonably dangerous to the user or consumer or to his property is subject to liability for physical harm thereby caused to the ultimate user or consumer, or to his property, if
>
> (a) the seller is engaged in the business of selling such a product, and
>
> (b) it is expected to and does reach the user or consumer without substantial change in the condition in which it is sold.
>
> (2) The rule stated in Subsection (1) applies although

> (a) the seller has exercised all possible care in the preparation and sale of his product, and
>
> (b) the user or consumer has not bought the product from or entered into any contractual relation with the seller.

Under the doctrine of strict products liability, manufacturers and sellers of products are held liable because society considers them better able than individuals to bear the costs of injuries and damage resulting from defective products. *See* **W. Page Keeton et al., Prosser and Keeton on Torts** § 98, at 692-93 (5th ed. 1984) [hereinafter **Prosser & Keeton**] (manufacturers and sellers "have the capacity to distribute the losses of the few among the many who purchase the products"); *Greenman v. Yuba Power Prods., Inc.*, 59 Cal.2d 57, 377 P.2d 897 (1963); **Thomas J. Schoenbaum, Admiralty and Maritime Law** § 5-6, at 177 (1994) (policies underlying strict liability apply in admiralty).

A

Martinac and Marco argue, based on two theories, that the district court erred in concluding that they owed any duty to Saratoga Fishing. They contend first that Saratoga Fishing was a sophisticated commercial buyer and that imposition of a strict products liability duty in this context is unwarranted. Next, Martinac and Marco argue that Saratoga Fishing failed to establish that the vessel, specifically the hydraulic system, was without substantial change. Thus, they contend that under Restatement section 402A(1)(b), they had no duty to protect

Saratoga Fishing from a defective condition unreasonably dangerous to it.[3]

Marco and Martinac raise interesting policy arguments for why commercial sellers should not owe a strict products liability duty to sophisticated commercial buyers of products such as fishing vessels. Many of the concerns animating strict products liability, including the ability of manufacturers and sellers to better absorb the costs of defective products, do not necessarily support strict products liability in this context. Indeed, private insurance on the part of the vessel's owner would, it is argued, provide a more effective economic allocation of risk. We have also recognized that section 402A of the Restatement "should be applied only when the purposes it seeks to serve dictate its application." *McKay v. Rockwell Int'l Corp.* 704 F.2d 444, 447 (9th Cir. 1983), *cert. denied*, 464 U.S. 1043 (1984).

[2] The question is not, however, an open one in this circuit. We have held a commercial seller of a maritime product strictly liable under Restatement section 402A in a factually similar case involving a presumably sophisticated commercial buyer. *Pan-Alaska*, 565 F.2d at 1134-37; *see also East River*, 476 U.S. 864-66, 871 (discussing application of strict products liability to "manufacturer in a commercial relationship"). Although we have not specifically considered the policy arguments raised here, we have yet to create an exception to strict products liability for certain sellers based on the commercial

[3]Marco and Martinac also argue that the trial court erroneously found that they had a duty to provide a "safe vessel." We agree that their duty was to provide a vessel that was not unreasonably dangerous to the user. In our judgment, however, the district court's choice of words in one finding does not undermine the propriety of its analysis of the appropriate nature of Marco and Martinac's duty.

nature of the sale.[4] *See* Paul N. Wonacott, *Products Liabilities of Shipbuilders and Repairers*, 62 Tulane L. Rev. 465, 469 (1988) (liability for a defective product under section 402A attaches in admiralty regardless whether "the accident-causing product is a structure uniquely designed to a particular owner's specifications"). Because many maritime transactions occur between commercial sellers and sophisticated buyers, the position advocated by Marco and Martinac would tend to eliminate what we have already accepted—that strict products liability is a part of the general maritime law.

Marco and Martinac's other argument regarding strict products liability duty is also unavailing. They misperceive the meaning of "substantial change" as defined by section 402A(1)(b). The Restatement section 402A provides that the product must "reach the user or consumer without substantial change in the condition in which it is sold." Thus, if a manufacturer's product is altered by a seller or other intermediary, the manufacturer might be immune from strict liability. *See* Restatement § 402A cmt. p. Once the product has reached the "user or consumer," however, that element has been satisfied. *See Emerson G.M. Diesel, Inc. v. Alaskan Enter.*, 732 F.2d 1468, 1475 (9th Cir. 1984) (product must not be "altered or changed when it reached the consumer"), *overruled in part on other grounds by East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858 (1986).

[4]In *McKay*, 704 F.2d at 447 n.4, we recognized those limited circumstances when strict products liability does not apply. They include unavoidably unsafe products, used products and services. We also added to that list in *McKay* that only in limited circumstances should a manufacturer be held strictly liable in tort for injuries to a service member in active duty caused by a design defect in military equipment. *Id.* at 447-48.

[3] Any misuse or fault by the user or consumer could and indeed, in this case, did reduce the plaintiff's recovery. Restatement § 402A cmt. n; *Pan-Alaska*, 565 F.2d at 1138 (comparative fault concepts can be applied to strict products liability). Whether the plaintiff misused the product, or significantly altered the product so as to become an intervening, superseding proximate cause of the resulting loss may even relieve the manufacturer or seller from liability altogether, but that misuse or alteration does not relate to whether the manufacturer or seller had a duty to the consumer or user. The duty exists if the product was in a defective condition at the time the consumer or user obtained the product. Because the hydraulic system retained the same design when Saratoga Fishing acquired the product from Madruga in 1974 as it did when Marco and Martinac installed the system, Marco and Martinac owe a duty to Saratoga Fishing regarding any design defect.

[4] In any case, the alterations made to the hydraulic system by Saratoga Fishing did not substantially alter the design of the system, which is what the district court found to be defective. The design of the system was the same on the day of the vessel's loss as it was when the SARATOGA left the shipyard.

B

Martinac and Marco argue that the district court erred in finding the design of the hydraulic system to be defective. They contend that the district court improperly applied a risk-utility test instead of a consumer or user expectations test to determine if the hydraulic system was defectively designed. Finally, Marco and Martinac argue, the district court misapplied the risk-utility test. We disagree with each of these contentions.

Admiralty courts use two methods to determine whether a product is defectively designed. The first method, drawn from Restatement section 402A comment i, provides that a product is defective if it is "dangerous to an extent beyond that which would be contemplated by the ordinary consumer who purchases it, with the ordinary knowledge common to the community as to its characteristics." This is the consumer expectations test. *See* Wonacott, *Shipbuilder Liability*, at 469; **Prosser & Keeton** § 99, at 698.

Although utilized by many courts, this test has come under criticism because of several shortcomings. First, it allows a manufacturer or seller to escape liability when the unreasonable danger is open and obvious. *See* **Prosser & Keeton** § 99, at 698-99; **M. Stuart Madden, Products Liability** § 6.7, at 213-14 (1988). Second, it is unpredictable in application. *See* **Prosser & Keeton** § 99, at 699. Because of the weaknesses of this test, some courts have sought an alternative way to determine whether a product was defectively designed.

A second test evolved from Judge Learned Hand's balancing test in a negligence case, *United States v. Carroll Towing Co.*, 159 F.2d 169, 173 (2d Cir. 1947). The risk-utility balancing test, in the context of a strict products liability action, weighs the utility of the product against the gravity of the danger. If, after considering the utility of the product, the economic and practical feasibility of alternative designs, and the gravity and likelihood of the potential harm, the factfinder determines that the risk outweighs the utility, the product is deemed defective or unreasonably dangerous.[6] *See Pavlides v.*

[6] In a design defect case, the terms "defective condition" and "unreasonably dangerous" arguably share a common meaning. *See Hagans v. Oliver Mach. Co.*, 576 F.2d 97, 99 n.4 (5th Cir. 1978) (stating that "[a]s used in the Restatement" the two terms are synonymous); *see also* Carl T. Bogus, *Pistols, Politics & Products Liability*, 59 U. Cin. L.

Galveston Yacht Basin, Inc., 727 F.2d 330, 337 (5th Cir. 1984) (applying risk-utility test in admiralty case); *Borel v. Fibreboard Paper Prods. Corp.*, 493 F.2d 1076, 1078 (5th Cir. 1973) (nonadmiralty case), *cert. denied*, 419 U.S. 869 (1974); Wonacott, *Shipbuilder Liability*, at 469; **Prosser & Keeton § 99**, at 699-700.

[5] A recent law review article noted that "[a]dmiralty decisions reveal that no predictable fact pattern or particular liability theory will dictate application of any one test; so it is not believed possible to identify a consistently preferred admiralty standard." Wonacott, *Shipbuilder Liability*, at 471. The language of section 402A neither compels nor precludes the application of either test; it merely provides for an examination of whether a product is unreasonably dangerous.

We have not indicated which test or tests should be applied in admiralty cases in this circuit.[6] The district court rejected the pure application of the "so-called consumer's expectations" test in comments g and i of Restatement section 402A. Instead, the court applied the risk-utility test, citing the

Rev. 1103, 1107-08 (1991) (arguing that in design defect cases, unreasonable danger is synonymous with defective condition); David P. Griffith, Note, *Products Liability—Negligence Presumed: An Evolution*, 67 Tex. L. Rev. 851, 859-60, 860 n.50 (1989) (citing sources supporting proposition that "defective" and "unreasonably dangerous" are synonymous and will lead to the same conclusion in design defect cases). Although we need not hold that the two terms will be synonymous in all cases, we use the terms interchangeably here. In other words, under either the consumer expectations test or the risk-utility test, a product that is deemed unreasonably dangerous will also be deemed to be in a defective condition. Conversely, a product in a defective condition must also be unreasonably dangerous.

[6]Marco and Martinac rely on *McCune v. F. Alioto Fish Co.*, 597 F.2d 1244 (9th Cir. 1979) and *Complaint of Diehl*, 610 F. Supp. 223 (Idaho

Fifth Circuit's decision in *Pavlides*. The district court proceeded to examine the risk and utility of the design along with the feasibility of alternative designs.

[6] We agree with the district court regarding the appropriateness of applying the risk-utility test in this case. If the consumer expectations test had been applied, the danger posed by the placement of the hoses of the hydraulic system in close proximity to the hot engine and turbocharger surfaces would likely be deemed open and obvious, especially to a purchaser or user of a fishing vessel. We are not satisfied with the possibility that a product with a design having high risk and limited utility, and a design that has other feasible alternatives, could be found not to be unreasonably dangerous or defective merely because a consumer, using the product in a foreseeable way, could recognize the danger.[7] As the district court correctly recognized, the risk-utility test provides a superior yardstick of whether a product is unreasonably dangerous or defective.

[7] We note that a preliminary draft of the Restatement (Third) of Torts by the reporters for the American Law Institute relies on a risk-utility analysis for deciding design defect cases. *See* Restatement (Third) of Torts: Products Liability § 2 (Tentative Draft No. 1, 1994). The tentative draft divides

1985), to support their argument that only a consumer expectations test should be applied in admiralty. Neither case supports that proposition. *McCune* merely affirmed, without discussion, a district court's finding that a product was not defective. *Diehl*, which is a district court decision, did apply a consumer expectations test in the context of an admiralty case, but it did not discuss, and it certainly did not preclude, the applicability of other tests.

[7]Neither party argued that the product in this case was an unavoidably unsafe product. *See* Restatement § 402A cmt. k.

defective product cases into three categories: manufacturing defect cases, design defect cases, and inadequate warning cases. Proposed section 2(b) provides that "[a] product is defective in design when the foreseeable risks of harm posed by the product could have been reduced by the adoption of a reasonable alternative design by the seller . . . and the omission of the alternative design renders the product not reasonably safe." *Id.* § 2(b). Under the proposed Restatement, the consumer expectations test no longer "constitute[s] an independent standard for judging the defectiveness of product designs." *Id.* § 2(b) cmt. e. Instead, the focus is on the reasonableness of the design and the plaintiff's ability to prove that a reasonable alternative design would have reduced foreseeable risks of harm. *Id.* § 2(b) cmt. c. Although we need not, and do not, adopt the formulation of the Restatement (Third) at this time, it provides support for our holding that a focus on the design's benefits, risks, and feasible alternatives is a better approach to examining an alleged design defect. *See id.* § 2(b) cmt. c, reporters' note at 41 ("[s]cholarly commentary agrees overwhelmingly with . . . the risk-utility approach.").

[8] Our approval of an application of the risk-utility test in this case does not necessarily preclude future admiralty plaintiffs from showing a design defect using the consumer expectations test. In *Pan-Alaska*, we adopted the Restatement § 402A as the law of this circuit. That section includes comment i, which allows a consumer to show that a product was unreasonably dangerous in a way not contemplated by the consumer. Other jurisdictions permit a plaintiff to show a product design defect under either approach. *See, e.g., Barker v. Lull Engineering Co.*, 20 Cal.3d 413, 432, 573 P.2d 443 (1978); *Caterpillar Tractor Co. v. Beck*, 593 P.2d 871, 884 (Alaska 1979). Given our traditional discretion in admiralty, *see East River*, 476 U.S. at 871, we conclude that giving plaintiffs such a choice is appropriate.

Marco and Martinac next maintain that the district court improperly applied the risk-utility test because it failed to balance the various factors and failed to find that a feasible alternative design would have prevented the fire. Marco and Martinac also argue that the district court erred in finding the design unreasonably dangerous. We disagree.

[9] The district court examined the risk from the design of the hydraulic system, and found it extremely high. Saratoga Fishing presented evidence that hydraulic hoses can fail for a variety of reasons and that any failure under the currently designed system would lead to a serious fire. The district court considered the utility of the current design, but was persuaded that an alternative design, namely a metal shield placed to isolate the hot surfaces of the engine and turbocharger from the hydraulic hoses, would have led to less "harmful consequences."

[10] The district court did not rely on the mere technical possibility of a safer design. *See Glover v. BIC Corp.*, 987 F.2d 1410, 1422-23 (9th Cir.), *amended*, 6 F.3d 1318 (9th Cir. 1993). Rather, Saratoga Fishing presented evidence regarding specific feasible improvements in design. Indeed, Mr. Martinac himself testified that Martinac "now puts up a sheet metal barrier" in vessels. A barrier could have isolated the hydraulic hoses from the turbocharger and engine surfaces, while maintaining the utility of the system. Although the district court found that Marco and Martinac's failure to use such a shield at the time of construction did not violate any industry rules or standards, it found the design unreasonably dangerous and defective because the design included a high risk of danger and there was a feasible alternative.

[11] Many qualified experts testified on both sides regarding the efficacy of the hydraulic system's design and the fea-

sibility and safety of other designs. The parties disagree on whose experts and evidence deserve credence, as the experts disagreed on many critical issues, including whether the design was defective. We must accord due deference to the district court's consideration of the experts' testimony and the court's findings regarding that testimony. *Anderson v. City of Bessemer City*, 470 U.S. 564, 573-75 (1985) (citing Fed. R. Civ. P. 52(a)) ("[w]here there are two permissible views of the evidence, the factfinder's choice between them cannot be clearly erroneous."). The district court correctly applied the risk-utility test in finding the design of the hydraulic system defective. Its findings are not clearly erroneous.[8]

C

Marco and Martinac argue that the district court erred in finding that Saratoga Fishing's misuse and alteration of the hydraulic system was not a superseding cause of the accident and subsequent loss of the vessel. Again, we disagree.

Any design defect must be shown to have contributed to, or caused the accident that led to the injury. *Matthews v. Hyster Co.*, 854 F.2d 1166, 1168 (9th Cir. 1988); **Prosser & Keeton** § 102, at 710-11 ("product defect under strict liability must be a proximate cause of claimant's injury"). Here, the

[8]Although Saratoga Fishing contends that the district court also found Marco and Martinac negligent, the district court's findings and conclusions indicate that the only basis for its holding was strict products liability. The court's mention of negligence in a few places is not sufficient to establish a finding of liability. If the district court did intend to reach a negligence decision, it did not set forth negligence law or make findings regarding that law. Further, it did not address the critical issue in negligence, the fault of the defendant. It addressed only the unreasonably dangerous nature of the product. Thus, any conclusion of negligence is unsupported.

presence of the hydraulic hoses near the hot engine and turbocharger surfaces without any effective shield was undoubtedly a proximate cause of and contributed to the fire that resulted in the vessel's loss. The district court found that this was the case, and this finding is not clearly erroneous.

Notwithstanding the existence of proximate cause, a manufacturer of a defective product can still be relieved of liability if some unforeseeable misuse or alteration occurred rising to the level of a superseding cause. **Prosser & Keeton** § 102, at 711. Marco and Martinac argue that such unforeseeable conduct occurred here.

They initially rely on a district court finding where the court purportedly stated that Saratoga Fishing's actions were a "precipitating cause" of the vessel's loss. Although the district court did make this finding, Marco and Martinac take it out of context. The court actually found that Saratoga Fishing's poor maintenance, misuse, and modifications to the hydraulic system "all contributed in some part to cause and bring about the catastrophic fire which ignited in the upper engine room . . . and was the precipitating cause of the vessel's loss . . . ." As this longer excerpt reveals, the court found that the fire was the precipitating cause of the loss. This is, of course, obvious. The court did not find that Saratoga Fishing's actions were a precipitating cause of the fire, rather it found that they were a contributing, or "substantial cause[ ]" of the fire.

[12] The district court did not find that Saratoga Fishing's misuse and alteration of the hydraulic system amounted to a superseding cause of the accident. The district court could have, but did not, find Saratoga Fishing's misuse to be

unforeseeable.[9] *Cf. Kay v. Cessna Aircraft Co.*, 548 F.2d 1370, 1372-73 (9th Cir. 1977) (plaintiff may recover if product is used in foreseeable, even if unintended use). The district court instead decided that hydraulic hose failure through either misuse, poor maintenance, or other conduct was foreseeable to Marco and Martinac, and that it would operate to reduce Saratoga Fishing's recovery but not to supersede Marco and Martinac's design defect as a proximate cause of the loss. This finding was not clearly erroneous.

[13] Marco and Martinac point to the alterations in the hydraulic system as examples that the system was modified substantially. The modifications, however, did not alter the design to the point where they superseded the design as a proximate cause of the fire.

D

Saratoga Fishing argues that the district court erred in reducing its award of damages by two-thirds based on the court's findings that it was also at fault for altering, misusing, failing to properly maintain, and ignoring the imminent failure of the hydraulic system. We agree with the district court.

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[9]There was some controversy at trial over a water shield that was ostensibly installed over the turbocharger at the time the hydraulic system was installed on the SARATOGA. The district court was unable to determine whether this shield had been removed. It found however, that even if this shield had been in place, it would not have prevented the fire from igniting because it did not adequately cover the surfaces of the turbocharger and engine or isolate the hydraulic hoses from the surfaces. These findings are not clearly erroneous, and thus the presence or absence of the water shield does not affect Martinac and Marco's liability or affect whether Saratoga Fishing's actions constituted a superseding cause of the accident.

We have held that the concepts of "comparative fault (i.e., contributory negligence) . . . can be applied to the doctrine of strict products liability." *Pan-Alaska*, 565 F.2d at 1138. Under comparative fault principles, a party's blameworthy conduct that contributes to the proximate cause of the loss or injury will be compared to the defendant's liability and act to reduce the plaintiff's award of damages. *Id.* at 1139-40. As we stated: "It comes down to this: the defendant is strictly liable for the harm caused from his defective product, except that the award of damages shall be reduced in proportion to the plaintiff's contribution to his own loss or injury." *Id.* at 1139.

The district court found that Captain Vargas failed to properly maintain the hydraulic system. In an effort to increase the speed and power of the system, Vargas authorized enlarging the size of the seine, increasing the size of the power block, and increasing the velocity of the hydraulic flow and power to the machinery and equipment. This increased velocity raised the temperature of the hydraulic fluid and resulted in increased deterioration of the component parts of the hydraulic system, including the hydraulic hoses.

The district court also found that the engineers on board informed Captain Vargas that the hydraulic system was "overworked, wearing out and prone to an increasing number of failures." Vargas nonetheless continued to operate the system in excess of design pressures and temperatures and deferred remedial measures. Most significantly, the district court found that on January 16, the hydraulic hose that eventually failed was observed by the Chief Engineer and his assistant to be "leaking or weeping at the coupling."[10] Despite

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[10]Although Chief Engineer Nielson testified that he did not consider the defective hose to be dangerous, the district court found that the engineer must have been aware that it needed replacing and that the hydraulic system should not be operated. The district court also rejected Nielson's testimony that he was unaware of a risk of danger.

being informed of the problem with the hose, Captain Vargas continued to operate the hydraulic system. The district court found that this created an "unreasonable risk that the hose would fail," causing hydraulic fluid to come in contact with the surface of the engine.

[14] The poor maintenance of the system, the modifications to the system, and the use of the system known to have a defective hose all contributed to the fire that caused the sinking of the vessel. The district court found that the conduct of those who manned the SARATOGA "border[ed] on irresponsible." The district judge is in the best position to weigh the evidence and apportion fault. *Alkmeon Naviera, S.A. v. M/V Marina L*, 633 F.2d 789, 796 (9th Cir. 1980). The district court's determination is not clearly erroneous and the apportionment of two-thirds liability to Saratoga Fishing will not be disturbed.

Saratoga Fishing next argues that Marco and Martinac failed to establish the standard of care of a prudent tuna boat operator. We reject this argument. Marco and Martinac presented substantial evidence concerning proper maintenance and care of a fishing vessel's hydraulic system. That is more than sufficient to establish a standard of care.

IV

We next address the subject of damages. The district court awarded Saratoga Fishing $452,326, which sum equals one-third of the combined value of the following items: the tuna catch, net, skiff, fuel, assorted equipment, crew losses, rescue costs, and cash. The district court declined to award damages for the value of replacement parts and the vessel's hull. Marco, Martinac, and Saratoga Fishing raise various objections to the award. With one exception, we reject each of the arguments and agree with the district court's determinations.

[15] In *East River S.S. Corp v. Transamerica Delaval Inc.*, 476 U.S. 858 (1986), the Supreme Court recognized a significant limitation to its decision to adopt the law of strict products liability to admiralty. The Court drew a distinction between damage caused to the "product itself" and damage to a "person or other property." *Id.* at 870. When the product itself is damaged, the "resulting loss is purely economic" and losses such as "repair costs, decreased value, and lost profits . . . essentially [involve] the failure of the purchaser to receive the benefit of its bargain—traditionally the core concern of contract law." *Id.* At least in the commercial context, the Court stated that damage to a product should be sought by plaintiffs through a contract or warranty claim. A cause of action for damages in a products liability claim in admiralty is available only for an injury to persons or "other property." *Id.*

We have not yet had the opportunity to further define the contours of "other property." The Fifth Circuit has developed some principles in this area. In *Shipco 2295, Inc. v. Avondale Shipyards, Inc.*, 825 F.2d 925 (5th Cir. 1987), the Fifth Circuit was faced with the question whether the "product" consisted of a finished vessel or individual components that were included in the vessel. That court focused on the perspective of the buyer of the vessel, and held that the finished vessel that was the "object of the contract must be considered 'the product' rather than the individual components that make up the vessel[ ]." *Id.* at 928. The Fifth Circuit added that "the product in this context means the finished product bargained for by the buyer rather than components furnished by a supplier." *Id.* at 930.

A

We are faced here with a slightly different situation. The

vessel that Martinac sold to Madruga constituted the "product" as far as Madruga was concerned. We must decide whether the "product" changed when Madruga added various components, including a skiff, seine and other miscellaneous parts, to the vessel and resold it to Saratoga Fishing.

We are guided by the policies set forth in *East River*, where the Court stated that the focus of the product should be on the failure of the purchaser to receive the benefit of its bargain. Warranty and contract law are appropriate for this type of situation. Here, the purchaser is Saratoga Fishing and the object of its bargain was the M/V SARATOGA with the components already installed. Saratoga Fishing purchased the vessel "as is." Madruga made no "warranty or representation of vessel condition."

The Fifth Circuit's decision in *Nicor Supply Ships Assoc. v. General Motors*, 876 F.2d 501 (5th Cir. 1989) is not in conflict with this principle. In that case, the vessel was sold only once. The buyer then time-chartered the vessel to a third-party, who installed equipment on the vessel. The court properly focused on the bargain between the buyer and shipbuilder to determine what was the product. *Id.* at 505-06. The equipment was deemed "other property."

East River provides a situation more similar to the one we confront here. In that case, the shipbuilder sold the vessel to a purchaser who subsequently executed an agreement with a bareboat charterer. The charterer took the vessel in an "as is" condition and assumed full responsibility for the vessel including maintenance, repair and insurance. 476 U.S. at 875. The Supreme Court focused on the terms of "the charterers' agreements with the owners." *Id.* The Court also noted that the "contractual responsibilities thus were clearly laid out. There is no reason to extricate the parties from their bargain." *Id.* The contract being discussed is that between the first

buyer and the bareboat charterer, who the Court treated as equivalent to a second buyer.

[16] Saratoga Fishing is the second buyer in this case. We must therefore focus on its agreement with Madruga. We see no reason to extricate Saratoga Fishing from its bargain. The parties chose not to include a seller's warranty, and we will not second guess their choice. The "product" in this case is the vessel that was delivered to Saratoga Fishing. Because it included the skiff, net, fuel, spare parts, and miscellaneous equipment, those items are part of the product and are not recoverable in a tort action as "other property."

It would indeed be anomalous for the shipbuilder's liability to increase every time the vessel was modified and resold. We agree with Marco and Martinac that such a result is inconsistent with *East River* and with the policies behind the application of products liability law to admiralty. The district court's award of damages to Saratoga Fishing for the skiff, net, fuel, spare parts, and miscellaneous equipment installed on the SARATOGA when it was sold to Saratoga Fishing is reversed.

Marco and Martinac next argue that an award of damages for the tuna catch was unjustified. They contend that the lost catch was a nonrecoverable pure economic loss under various theories: first, because the lost catch was a work in progress; second, because the lost catch was equivalent to damaged cargo; and third because it was similar to failed or damaged crops. We disagree.

[17] The tuna catch that was destroyed was different than cargo because it was not being shipped from one site to another pursuant to a commercial agreement. It was new property on board the SARATOGA that belonged to the vessel's owner. The tuna was also not a work in progress as it

had substantial value after being caught. The district court correctly reduced the value of the tuna by accounting for fuel costs and Panama Canal toll charges, and accurately computed the value of the tuna lying in the holds of the SARATOGA. Finally, the cases involving damaged crops are agricultural cases and are not helpful in the context of admiralty. We conclude that the tuna catch was not an economic loss, but was a loss of other property. The district court did not abuse its discretion in awarding damages for the tuna catch.

Marco and Martinac lastly contend that the district court erred in awarding Saratoga Fishing the value of Captain Vargas' lost currency because it was duplicative of sums awarded under the category of the lost crew property. The district court found that Vargas' testimony was "not effectively refuted" and was "credible." Marco and Martinac have shown insufficient evidence that the district court's findings were clearly erroneous. We will not disturb them.

B

Saratoga Fishing appeals the district court's refusal to award the value of replacement equipment installed in the vessel. It also argues that the district court erred in not permitting it to include the value of the vessel's hull in its damages sought from Marco.

[18] The district court concluded that replacement parts should not be recoverable as "other property" under *East River*. The court stated that permitting recovery would lead to the absurd result that the shipbuilder's liability would grow as the performance of the product's relationship to the shipbuilder decreased. We agree. Because a product may have any number of components replaced with spare parts in the ordi-

nary course of events, viewing these parts as "other property" would lead to absurd results. Such results would be contrary to the policies of *East River*, where the Supreme Court expressed its intention to exclude damages to the product itself from tort law and leave the injured party to remedies in the law of contract and warranty. 476 U.S. at 871-72; *see Exxon Shipping Co. v. Pacific Resources, Inc.*, 835 F. Supp. 1195, 1200 (D. Haw. 1993) (prohibiting recovery of cost of replacement parts in admiralty products liability action).

Saratoga Fishing lastly seeks damages from Marco (not Martinac) for the loss of the vessel itself. This argument is based on two propositions: first, that the approach to damages in *East River* should not apply to fishermen; and second, that for a component manufacturer such as Marco, the only "product" is its hydraulic system and that the vessel is "other property." Neither argument has merit.

Saratoga Fishing relies on footnote 5 in *East River*, in which the Supreme Court observed that it had at times applied a more protective approach in some admiralty contexts for fishermen, and that no fishermen were involved in that case. Even if that footnote reflected an exception to the rules set forth in *East River*, it is not applicable here. Saratoga Fishing is a company that owned an ocean-going tuna fishing vessel; there are no individual fishermen involved in this litigation. In any case, the only court that has considered the effect, if any, of the footnote, applied the *East River* damages rules without exception to a case involving plaintiffs who were fishermen. *McConnell v. Caterpillar Tractor Co.*, 646 F. Supp. 1520, 1525 (D.N.J. 1986).

Also without merit is Saratoga Fishing's argument that the vessel should be deemed "other property" relative to Marco because Marco designed a component part of the vessel. The

Fifth Circuit has rejected a similar claim. In *Shipco 2295, Inc. v. Avondale Shipyards, Inc.*, 825 F.2d 925, 928 (5th Cir. 1987), *cert. denied*, 485 U.S. 1007 (1988), the Fifth Circuit rejected a damages claim against the designer of a component part, observing that there is "no rational reason to give the buyer greater rights to recover economic losses for a defect in the product because the component is designed, constructed or furnished by someone other than the final manufacturer." *Id.* at 929.

[19] This rationale is sound. Saratoga Fishing bargained for a fishing vessel. That is the product. The hydraulic system is an integral part of the product. Seldom does one company design and build all component parts for an integrated product such as a fishing vessel. Indeed, Saratoga Fishing, as we noted above, bargained with Madruga, not Martinac, for the vessel, so Saratoga Fishing was one step removed from the initial purchase. Even if Madruga had sought recovery for the hull, however, it would make no difference. Permitting recovery from Marco for the vessel's hull would undermine the policy of *East River*—namely, that contract and warranty law should cover such losses, while tort law should be reserved for "other property."

C

Marco and Martinac argue that the district court erred in awarding prejudgment interest to Saratoga Fishing. They contend that Saratoga Fishing delayed filing a claim for almost two years after the vessel's loss and that Saratoga Fishing further delayed the litigation during a dispute over an attorney's conflict of interest.[11]

[11]Although Marco and Martinac initially objected to an award of prejudgment interest because of the high degree of Saratoga Fishing's comparative fault, they abandoned that ground on appeal.

"In admiralty, prejudgment interest must be granted unless peculiar circumstances justify its denial." *McKay v. Rockwell Int'l Corp.*, 704 F.2d 444, 463 (9th Cir. 1983), *cert. denied*, 464 U.S. 1043 (1984). The determination of whether peculiar circumstances exist is left to the district court's sound discretion. *Id.* at 464.

[20] Here, the district court concluded that this case was not "sufficiently peculiar or exceptional to justify departure from the general rule." Saratoga Fishing's claim was filed within the statute of limitations; thus, any delay was certainly not peculiar or unusual. The attorney conflict is also not an unusual occurrence. There is insufficient reason to disturb the district court's exercise of its sound discretion in awarding prejudgment interest.

Marco and Martinac also object to the district court's purported computation of postjudgment interest as inconsistent with the statutory mandate of 28 U.S.C. § 1961. Saratoga Fishing correctly points out, however, that the district court did not award postjudgment interest. It awarded additional prejudgment interest from the date of the damages findings and conclusions, June 1, 1993, until the date of final judgment, August 27, 1993. We find no error with the decision to award additional prejudgment interest. Of course, in light of our decision reversing part of the damages award, the district court should recompute the entire award of prejudgment interest on remand.

Finally, Saratoga Fishing is entitled to a further award of interest pursuant to 28 U.S.C. § 1961 from the date of entry of judgment until payment is made.

V

We are persuaded that the district court, having heard from all the experts and witnesses, did not, with the one aforementioned exception, err in deciding the issues of liability and damages. Marco and Martinac will pay their share because of their defectively designed hydraulic system, but Saratoga Fishing's award will be substantially reduced because of its failure to properly maintain and operate that system.

On remand the district court is directed to reconsider the amount of damages and interest and to enter judgment accordingly.

AFFIRMED in part, REVERSED in part and REMANDED. Each party shall bear its own costs.

NOONAN, Circuit Judge, concurring and dissenting:

I concur in the opinion of the court, except as to its exclusion of damages for the skiff, seine net, fuel, spare parts and other miscellaneous equipment sold by Madruga to Saratoga Fishing as part of the sale of the M/V SARATOGA. None of this property was manufactured or sold by Martinac. Under *East River*, 476 U.S. 858, 867 all of it was "other property," damages for which are recoverable in tort. The court abandons *East River* and puts this circuit in conflict with another major maritime circuit, *Nicor Supply Ships Associates v. General Motors*, 876 F.2d 501, 505-06 (5th Cir. 1989). The opinion also repudiates controlling authority in this circuit, *Pan-Alaska Fisheries, Inc. v. Marine Construction & Design Co.*, 565 F.2d 1129 (9th Cir. 1977). That case accepted "as the law of products liability in this circuit, at least for this case arising

in admiralty," the Restatement (Second) of Torts, § 402A. *Id.* at 1135. Under the Restatement, the original seller of a product in a defective condition that is unreasonably dangerous that has entered the stream of commerce is strictly liable to the ultimate consumer for physical harm caused to that consumer's property. Saratoga Fishing is here the ultimate consumer; Martinac is the original seller; the property damaged was Saratoga Fishing's and no more a part of the product sold by Martinac than was the tuna catch for which damages are granted.

The court appears to have been swayed by the consideration that additions made by a middleman could increase the original seller's liability. That of course is a risk the seller of an unreasonably dangerous, defective product takes. If the explosion had occurred while Madruga still owned the boat after adding the skiff and net, there is no doubt that Martinac would have been liable for those additional items. Martinac's exposure should not decrease because Madruga sold the ship to Saratoga Fishing. Whatever theory one adopts, the liability of the original seller may change as the ultimate consumer adds or subtracts property which can be affected by the defective product. The theory of strict liability holds that the seller is stuck whatever foreseeable damage to the consumer's other property his product causes.

APPENDIX C — OPINION AND ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT FILED AUGUST 4, 1995

FOR PUBLICATION

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

SARATOGA FISHING CO., *Plaintiff-Appellee,* v. MARCO SEATTLE INC., *Defendant-Appellant,* and J.M. MARTINAC & CO.; CATERPILLAR TRACTOR CO.; SOUTHWEST MARINE HARDWARE, INC., *Defendants.*	No. 93-56344 D.C. No. CV-87-01691-JMF ORDER AND OPINION
SARATOGA FISHING CO., *Plaintiff-Appellant,* v. MARCO SEATTLE INC.; SOUTHWEST MARINE HARDWARE, INC.; CATERPILLAR TRACTOR CO.; J.M. MARTINAC & CO., *Defendants-Appellees.*	No. 93-56368 D.C. No. CV-87-01691-JMF

Appendix C

SARATOGA FISHING CO., *Plaintiff-Appellee,* v. J.M. MARTINAC & CO., *Defendant-Appellant.*	No. 93-56501 D.C. No. CV-87-01691-JMF

Appeals from the United States District Court
for the Southern District of California
James M. Fitzgerald, Chief Judge, Presiding

Argued and Submitted
February 8, 1995—Pasadena, California

Filed April 25, 1995
Withdrawn August 4, 1995
Filed August 4, 1995

Before: Robert R. Beezer and John T. Noonan, Jr., Circuit Judges, and David Alan Ezra, District Judge.*

Opinion by Judge Beezer

SUMMARY

Admiralty and Marine/Torts/Products Liability

The court of appeals affirmed in part a district court judgment, reversed in part and remanded. The court held that the

*The Honorable David Alan Ezra, United States District Judge for the District of Hawaii, sitting by designation.

district court correctly applied the "risk-utility" test in a design defect product liability action against a shipbuilder and the designer of the vessel's hydraulic system.

The fishing vessel M/V SARATOGA was designed and built by appellant J.M. Martinac & Co. for Joseph Madruga. During the construction process, Martinac contracted with appellant Marco Seattle Inc. to design a hydraulic system. The system was installed by Martinac and inspected by Marco.

The vessel's captain, Manuel Vargas, took the vessel to Panama, where the vessel was outfitted with a seine and other fishing equipment. The vessel then commenced tuna fishing operations. The vessel was purchased from Madruga by appellee Saratoga Fishing Co. As captain, Vargas ordered a series of modifications to various machinery and equipment: the size of the seine was increased; a larger boom and power block were installed; larger cartridges were installed in the pumps; and a 100-horsepower electric drive and pump were installed to increase power to the hydraulic system.

The Chief Engineer noticed that the hydraulic system was experiencing failures, but Vargas continued to seek increased power to the hydraulic system. An Assistant Engineer observed worn out pump cartridges and an overloaded hydraulic system. A new Chief Engineer noticed more problems with the hydraulic system. Repair work was completed in Panama. The Chief Engineer later observed a hydraulic hose seeping hydraulic fluid, but Vargas did not shut down the hydraulic system. A hydraulic hose pulled out of its coupling and hydraulic fluid sprayed up and fell back onto the hot surface of the turbocharger. The fluid ignited, and a fire spread throughout the vessel. The SARATOGA sank.

Saratoga Fishing brought suit in the district court against

Martinac and Marco within the court's admiralty jurisdiction seeking recovery for property losses. Saratoga Fishing argued that the hydraulic system was defectively designed, and sought recovery under theories of strict liability, negligence and failure to warn. Saratoga Fishing offered the expert testimony of a naval architect, who testified that the Marco hydraulic drive system incorporated an unsafe design. In the architect's opinion, the hydraulic hoses were located too close to the hot surfaces of the engine and turbocharger. The architect noted that hydraulic hoses and couplings are prone to failure for a variety of reasons, and that the designer of the hydraulic system should have taken preventive measures such as relocating the hoses elsewhere, installing an electric instead of a diesel motor to reduce the risk of a fire developing from leaking hydraulic fluid, or isolating the hoses from the engine and turbocharger by the use of shielding.

Marco and Martinac argued that the vessel's design was not defective, that Saratoga Fishing failed to maintain the fire suppression system or the hydraulic hoses, and that Saratoga Fishing had substantially altered and misused the hydraulic system. A marine architect testified that the hydraulic system on board the vessel met well-established marine practice, and that, in his opinion, the system was not operating properly because of the modifications made by Saratoga Fishing.

The district court concluded that Marco and Martinac were strictly liable for the loss of the SARATOGA. The court found that the hydraulic system was defectively designed despite the fact that it met established marine practices, and that the placement of the hydraulic hoses in close proximity to the engine and turbocharger presented a known serious risk of fire. The court found that feasible design changes, such as the placement of a shield to isolate the hydraulic hoses from the engine and turbocharger, would have reduced the risk.

The court found that the modifications made by Saratoga Fishing did not alter the chain of causation because they did not affect the design. The court applied the "risk-utility" test, examining the risk and utility of the design along with the feasibility of alternative designs.

The district court found, however, that Saratoga Fishing was at fault due to its poor maintenance of the hydraulic system, its overuse of the system, and its failure to recognize the signs of imminent failure of the system. Saratoga Fishing's comparative fault reduced its recovery by two-thirds. The award of damages to Saratoga Fishing included losses of the tuna catch, seine, skiff, fuel, equipment, the crews' personal losses, the cost of the rescue and Vargas' cash. The award did not include the loss of any replacement parts that Saratoga Fishing installed on the vessel or the loss of the vessel's hull. The court awarded prejudgment interest and additional interest to Saratoga Fishing until the date of the final judgment. Marco and Martinac appealed.

[1] The law of products liability, including strict liability, is recognized as part of the general maritime law. [2] The Ninth Circuit has held a commercial seller of a maritime product strictly liable under Restatement (Second) of Torts § 402A in a factually similar case involving a presumably sophisticated commercial buyer. [3] In addition, a plaintiff's misuse or alteration of a product does not relate to whether the manufacturer or seller had a duty to the consumer or user. [4] The alterations made to the hydraulic system by Saratoga Fishing did not substantially alter the design of the system.

[5] In regard to the determination of whether the product was defectively designed, the language of § 402A neither compelled nor precluded the application of either the risk-utility test or the "consumer expectations" test. [6] The

district court was correct regarding the appropriateness of appiying the risk-utility test in this case. If the consumer expectations test had been applied, the danger posed by the placement of the hoses of the hydraulic system in close proximity to the hot engine and turbocharger surfaces would likely have been deemed open and obvious. The risk-utility test provided a superior yardstick of whether the product was unreasonably dangerous or defective. [7] A focus on the design's benefits, risks, and feasible alternatives was a better approach to examining an alleged design defect. [8] However, the approval of an application of the risk-utility test in this case did not necessarily preclude future admiralty plaintiffs from showing a design defect using the consumer expectations test.

[9] The district court examined the risk from the design of the hydraulic system and found it to be extremely high. [10] The district court did not rely on the mere technical possibility of a safer design. [11] Due deference had to be given to the district court's consideration of the experts' testimony. Thus, the district court correctly applied the risk-utility test in finding the design of the hydraulic system defective.

[12] The district court did not find that Saratoga Fishing's misuse and alteration of the hydraulic system amounted to a superseding cause of the accident. [13] The alterations in the hydraulic system did not alter the design to the point where they superseded the design as a proximate cause of the fire.

[14] The poor maintenance of the hydraulic system, the modifications to the system and the use of the system known to have a defective hose all contributed to the fire that caused the sinking of the vessel. Thus, the apportionment of two-thirds liability to Saratoga Fishing was not disturbed.

[15] A cause of action for damages in a products liability

claim in admiralty is available only for injury to persons or "other property." [16] The "product" in this case was the vessel that was delivered to Saratoga Fishing. Because it included the skiff, net, fuel, spare parts, and miscellaneous equipment, those items were part of the product and were not recoverable in a tort action as "other property." [17] The tuna catch was not an economic loss, but was a loss of other property. Thus, the district court did not abuse its discretion in awarding damages for the tuna catch. [18] Because a product may have any number of components replaced with spare parts in the ordinary course of events, viewing these parts as "other property" would lead to absurd results. [19] Permitting recovery from Marco for the vessel's hull would undermine relevant policy.

[20] There was insufficient reason to disturb the district court's award of prejudgment interest.

COUNSEL

Daniel B. MacLeod, Alford & MacLeod, San Diego, California, for defendant-appellant-cross-appellee Marco Seattle, Inc. Duncan B. Koler, Walton, Ottesen, Meads & Koler, San Diego, California, for defendant-appellant-cross-appellee J.M. Martinac & Company.

Keith Zakarin, Pillsbury, Madison & Sutro, San Diego, California, for plaintiff-appellee-cross-appellant Saratoga Fishing Company.

ORDER

The panel has reviewed the petition for rehearing and suggestion for rehearing en banc. Upon further consideration, the petition for rehearing is granted. The opinion filed April 25, 1995, appearing at 53 F.2d 984 (1995), is hereby withdrawn and a new opinion is filed in its place. The balance of claims in the petition for rehearing are DENIED and the suggestion for rehearing en banc is REJECTED.

OPINION

BEEZER, Circuit Judge:

This products liability action in admiralty arose following an engine room fire that caused the flooding and sinking of the fishing vessel M/V SARATOGA. The district court concluded that J.M. Martinac & Company ("Martinac"), the shipbuilder, and Marco Seattle, Inc. ("Marco"), the designer of the vessel's hydraulic system, were strictly liable to Saratoga Fishing Company ("Saratoga Fishing"), the vessel owner, for damages to "other property" on the vessel because the fire and subsequent loss resulted from a defectively designed hydraulic system. The district court reduced the damages award by two-thirds, however, because of Saratoga Fishing's comparative fault in maintaining and operating that system. Both sides appeal the district court's determinations on liability and damages.[1]

We have jurisdiction over these timely appeals pursuant to 28 U.S.C. § 1291. Because we agree with all but one facet of the district court's resolution of this action, we affirm in part, reverse in part and remand.

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[1]Two other defendants, Caterpillar Tractor Company and Southwest Marine Hardware, Inc., are not parties to this appeal.

Appendix C

I

We retrace the fateful path of the fishing vessel M/V SARATOGA ("SARATOGA"). The vessel was designed and built in 1971 by Martinac in its Tacoma, Washington shipyards for Joseph Madruga. During the construction process, Martinac, after consulting with Madruga, contracted with Marco to design a hydraulic system. The system was installed by Martinac and inspected by Marco.

The SARATOGA's hydraulic system included pumps, pump drives, control valves, hoses and pressure gauges all connected to a 190-horsepower Caterpillar D333 engine and turbocharger. The system operated machinery and equipment such as a power block, a boom and winches, which were necessary to use the seine (net) for tuna fishing operations. Hydraulic fluid was pumped through the system to operate the deck machinery. The fluid exited the pumps through five rubber hoses attached to the pump drive by metal couplings. The hoses rose vertically from the pump to the overhead, passing near the engine and turbocharger.

The completed vessel was launched in 1972. Its captain, Manuel Vargas, took the vessel from San Diego, where it had undergone various sea trials, to Panama where she was outfitted with a seine and other fishing equipment. The SARATOGA then commenced tuna fishing operations.

In 1974, the Manuel S. Vargas, Jr. Corporation, which was principally owned by Vargas and later changed its name to Saratoga Fishing, purchased the SARATOGA from Madruga. At the time of sale, the vessel was equipped with five speedboats, a purse skiff, a seine, and various electronic equipment. Vargas continued to serve as captain until 1979.

Appendix C

When Vargas returned to the SARATOGA as captain in 1984, the condition of the vessel had deteriorated. While overseeing a refurbishing of the vessel, Vargas ordered a series of modifications to various machinery and equipment: the size of the seine was increased; a larger boom was installed; a larger power block was installed; larger cartridges were installed in the pumps; and a 100-horsepower electric drive and pump were installed to increase power to the hydraulic system above that of the original equipment.

A new Chief Engineer joined the vessel in 1984. Wesley Ogilvie noticed on his first fishing trip that the hydraulic system was experiencing failures, such as leaking valves and breaking hoses. Nevertheless, Captain Vargas continued to seek increased power to the hydraulic system to quicken the speed at which the seine could be pursed. Assistant Engineer Lewis Jorge joined the crew in 1985, and observed worn out pump cartridges and an overloaded hydraulic system. In late 1985, Ogilvie was replaced as Chief Engineer by Mark Nielson, who noticed more problems with the hydraulic system. Hydraulic hoses needed replacement, winches were leaking hydraulic fluid, and the temperature of the hydraulic fluid was abnormally high.

Various repair work was completed on the SARATOGA when she docked in Panama late in 1985, including the replacement of seals in the hydraulic system and pump cartridges. Workers also repaired damage to the turbocharger on the main engine. On January 8, 1986, the SARATOGA departed Panama to fish for tuna near the Gallapagos Islands in the Pacific Ocean.

On the afternoon of January 16, Chief Engineer Nielson observed one hydraulic hose seeping hydraulic fluid at the coupling attaching the hose to the pump. Although Captain Vargas arranged to rendezvous with another vessel to obtain a necessary tool to manufacture a replacement hose, Vargas did not shut down the hydraulic system. Instead, Vargas utilized the system to catch more tuna late that afternoon.

A short time later, Lewis Jorge entered the engine room and observed that a hydraulic hose was "pulsating." As Jorge watched, the hose pulled out of its coupling and hydraulic fluid sprayed up from the coupling and fell back onto the hot surface of the turbocharger. The fluid ignited causing an immediate conflagration in the engine room. Jorge and Nielson attempted to extinguish the fire, but their efforts were unsuccessful.

The fire quickly spread throughout the SARATOGA, and Captain Vargas ordered the crew to abandon ship. The crew left in a skiff, and were soon rescued by another vessel. No crew member suffered serious injury. Unfortunately, the SARATOGA sank.[2]

Property losses included, in addition to the loss of the vessel, all of the fishing equipment, fuel, a substantial tuna catch stored in the vessel, crew members' personal property losses, and $16,000 in cash that Captain Vargas had placed in the vessel's safe.

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[2]Although the district court found that the cause of the SARATOGA's sinking was the flooding that occurred as a consequence of the fire, it was unable to determine exactly how and why the flooding occurred. The district court determined that resolving that question was not necessary to its disposition. We agree.

Saratoga Fishing brought the instant lawsuit in district court against Martinac and Marco within the court's admiralty jurisdiction seeking recovery for property losses. *See* 28 U.S.C. § 1333. The court conducted a 14-day trial in which it heard testimony from a variety of expert witnesses and considered a substantial amount of evidence.

At trial, Saratoga Fishing argued that the hydraulic system was defectively designed. It sought recovery under theories of strict liability, negligence, and failure to warn.

Saratoga Fishing offered, among other witnesses, the expert testimony of David Saveker, a naval architect. Saveker testified that the Marco hydraulic drive system incorporated an unsafe design. The hydraulic hoses were, in Saveker's opinion, located too close to the hot surfaces of the engine and turbocharger. As hydraulic hoses and couplings are prone to fail for a variety of reasons, Saveker noted, the designer of the hydraulic system should have taken preventive measures such as relocating the hoses elsewhere, installing an electric instead of a diesel motor to reduce the risk of a fire developing from leaking hydraulic fluid, or isolating the hoses from the engine and turbocharger by the use of shielding. Such shielding would have "screen[ed] out a large percentage of the probability of an immediate torch" from the leaking hydraulic fluid. Saveker testified that the system was "a bad accident waiting to happen."

Marco and Martinac argued that the vessel's design was not defective, that Saratoga Fishing had failed to maintain the fire suppression system or the hydraulic hoses, and that Saratoga Fishing had substantially altered and misused the hydraulic system.

Larry Grief, a marine architect, testified as an expert wit-

ness for Marco and Martinac. He stated that the hydraulic system on board the SARATOGA met well-established marine practice and was similar to those on almost every vessel he had been aboard. The hydraulic hoses, Grief noted, were designed with a safety margin of 6 to 1 over standard operating pressures. In Grief's opinion, the hydraulic system was not operating properly because of the modifications made by Saratoga Fishing. The addition of a 100-horsepower electric drive caused the hydraulic fluid to pass through the system at a higher velocity, leading to a corresponding increase in the temperature of the hydraulic fluid, which in turn caused rapid deterioration. Furthermore, the larger equipment (seine, boom, and power block) installed by Saratoga Fishing required more hydraulic power, but the installation was not accompanied by any modifications in the hydraulic hoses.

The district court concluded that Marco and Martinac were strictly liable for the loss of the SARATOGA. The court found that the hydraulic system was defectively designed despite the fact that it met established marine practices. The placement of the hydraulic hoses in close proximity to the engine and turbocharger presented a known serious risk of fire and, the district court found, feasible design changes, such as the placement of a shield or barrier to isolate the hydraulic hoses from the engine and turbocharger, would have reduced the risk. The modifications made by Saratoga Fishing did not alter the chain of causation because they did not affect the design.

The court also found, however, that Saratoga Fishing was at fault due to its poor maintenance of the hydraulic system, its overuse of the system, and its failure to recognize the signs of imminent failure of the system. Saratoga Fishing's comparative fault reduced its recovery by two-thirds.

In a later ruling, the district court awarded damages to Saratoga Fishing in the amount of $452,326, one-third of the sum it determined to be Saratoga Fishing's total damages. The award included losses of the tuna catch, seine, skiff, fuel, equipment, the crews' personal losses, the cost of the rescue, and Captain Vargas' cash.

Not included in the award was the loss of any replacement parts that Saratoga Fishing installed on the vessel. The award also did not include the loss of the vessel's hull, which the trial court had decided pretrial was not recoverable from either defendant in an admiralty products liability action.

The court awarded prejudgment interest, which raised the total award to Saratoga Fishing to $734,940.38. Finally, the court awarded additional interest to Saratoga Fishing until the date of the final judgment at the rate of $153.09 per day.

II

We review the admiralty trial court's findings of fact for clear error, and its conclusions of law *de novo*. *Havens v. F/T Polar Mist*, 996 F.2d 215, 217 (9th Cir. 1993). The existence and extent of a duty are questions of law reviewed *de novo*, while proximate cause and whether such a duty has been breached are questions of fact reviewed for clear error. *Martinez v. Korea Shipping Corp.*, 903 F.2d 606, 609 (9th Cir. 1990).

We review *de novo* the legal conclusion that damages are available. *United States v. Timberland Paving & Constr. Co.*, 745 F.2d 595, 599 (9th Cir. 1984) ("[w]e review questions of law de novo"). Finally, we review for clear error a trial court's factual findings in support of an award for damages. *Bergen v. F/V St. Patrick*, 816 F.2d 1345, 1347 (9th Cir. 1987), *cert. denied*, 493 U.S. 871 (1989).

III

[1] Saratoga's claims fall within the admiralty jurisdiction, as they arose on the high seas. 28 U.S.C. § 1333; *see Jerome B. Grubart, Inc. v. Great Lakes Dredge & Dock Co.*, 115 S. Ct. 1043, 1047 (1995). We apply, as the district court did, substantive admiralty law, which, absent a federal statute, is the general maritime law. *East River S.S. Corp. v. Transamerica Delaval Inc.*, 476 U.S. 858, 864 (1986). The law of products liability, including strict liability, is recognized as part of the general maritime law. *Id.* at 865; *Pan-Alaska Fisheries, Inc. v. Marine Constr. & Design Co.*, 565 F.2d 1129, 1135 (9th Cir. 1977).

In holding that a strict products liability action would lie in admiralty, we adopted the Restatement (Second) of Torts § 402A (1965) as "the law of products liability in this circuit" because it was "the best and most widely-accepted expression of the theory of strict products liability." *Pan-Alaska*, 565 F.2d at 1135. Section 402A provides as follows:

> (1) One who sells any product in a defective condition unreasonably dangerous to the user or consumer or to his property is subject to liability for physical harm thereby caused to the ultimate user or consumer, or to his property, if
>
> (a) the seller is engaged in the business of selling such a product, and
>
> (b) it is expected to and does reach the user or consumer without substantial change in the condition in which it is sold.
>
> (2) The rule stated in Subsection (1) applies although

> (a) the seller has exercised all possible care in the preparation and sale of his product, and
>
> (b) the user or consumer has not bought the product from or entered into any contractual relation with the seller.

Under the doctrine of strict products liability, manufacturers and sellers of products are held liable because society considers them better able than individuals to bear the costs of injuries and damage resulting from defective products. *See* **W. Page Keeton et al., Prosser and Keeton on Torts** § 98, at 692-93 (5th ed. 1984) [hereinafter **Prosser & Keeton**] (manufacturers and sellers "have the capacity to distribute the losses of the few among the many who purchase the products"); *Greenman v. Yuba Power Prods., Inc.*, 59 Cal.2d 57, 377 P.2d 897 (1963); **Thomas J. Schoenbaum, Admiralty and Maritime Law** § 5-6, at 177 (1994) (policies underlying strict liability apply in admiralty).

A

Martinac and Marco argue, based on two theories, that the district court erred in concluding that they owed any duty to Saratoga Fishing. They contend first that Saratoga Fishing was a sophisticated commercial buyer and that imposition of a strict products liability duty in this context is unwarranted. Next, Martinac and Marco argue that Saratoga Fishing failed to establish that the vessel, specifically the hydraulic system, was without substantial change. Thus, they contend that under Restatement section 402A(1)(b), they had no duty to protect

Saratoga Fishing from a defective condition unreasonably dangerous to it.[3]

Marco and Martinac raise interesting policy arguments for why commercial sellers should not owe a strict products liability duty to sophisticated commercial buyers of products such as fishing vessels. Many of the concerns animating strict products liability, including the ability of manufacturers and sellers to better absorb the costs of defective products, do not necessarily support strict products liability in this context. Indeed, private insurance on the part of the vessel's owner would, it is argued, provide a more effective economic allocation of risk. We have also recognized that section 402A of the Restatement "should be applied only when the purposes it seeks to serve dictate its application." *McKay v. Rockwell Int'l Corp.*, 704 F.2d 444, 447 (9th Cir. 1983), *cert. denied*, 464 U.S. 1043 (1984).

[2] The question is not, however, an open one in this circuit. We have held a commercial seller of a maritime product strictly liable under Restatement section 402A in a factually similar case involving a presumably sophisticated commercial buyer. *Pan-Alaska*, 565 F.2d at 1134-37; *see also East River*, 476 U.S. 864-66, 871 (discussing application of strict products liability to "manufacturer in a commercial relationship"). Although we have not specifically considered the policy arguments raised here, we have yet to create an exception to strict products liability for certain sellers based on the commercial

[3]Marco and Martinac also argue that the trial court erroneously found that they had a duty to provide a "safe vessel." We agree that their duty was to provide a vessel that was not unreasonably dangerous to the user. In our judgment, however, the district court's choice of words in one finding does not undermine the propriety of its analysis of the appropriate nature of Marco and Martinac's duty.

nature of the sale.[4] *See* Paul N. Wonacott, *Products Liabilities of Shipbuilders and Repairers*, 62 Tulane L. Rev. 465, 469 (1988) (liability for a defective product under section 402A attaches in admiralty regardless whether "the accident-causing product is a structure uniquely designed to a particular owner's specifications"). Because many maritime transactions occur between commercial sellers and sophisticated buyers, the position advocated by Marco and Martinac would tend to eliminate what we have already accepted—that strict products liability is a part of the general maritime law.

Marco and Martinac's other argument regarding strict products liability duty is also unavailing. They misperceive the meaning of "substantial change" as defined by section 402A(1)(b). The Restatement section 402A provides that the product must "reach the user or consumer without substantial change in the condition in which it is sold." Thus, if a manufacturer's product is altered by a seller or other intermediary, the manufacturer might be immune from strict liability. *See* Restatement § 402A cmt. p. Once the product has reached the "user or consumer," however, that element has been satisfied. *See Emerson G.M. Diesel, Inc. v. Alaskan Enter.*, 732 F.2d 1468, 1475 (9th Cir. 1984) (product must not be "altered or changed when it reached the consumer"), *overruled in part on other grounds by East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858 (1986).

[4]In *McKay*, 704 F.2d at 447 n.4, we recognized those limited circumstances when strict products liability does not apply. They include unavoidably unsafe products, used products and services. We also added to that list in *McKay* that only in limited circumstances should a manufacturer be held strictly liable in tort for injuries to a service member in active duty caused by a design defect in military equipment. *Id.* at 447-48.

[3] Any misuse or fault by the user or consumer could and indeed, in this case, did reduce the plaintiff's recovery. Restatement § 402A cmt. n; *Pan-Alaska*, 565 F.2d at 1138 (comparative fault concepts can be applied to strict products liability). Whether the plaintiff misused the product, or significantly altered the product so as to become an intervening, superseding proximate cause of the resulting loss may even relieve the manufacturer or seller from liability altogether, but that misuse or alteration does not relate to whether the manufacturer or seller had a duty to the consumer or user. The duty exists if the product was in a defective condition at the time the consumer or user obtained the product. Because the hydraulic system retained the same design when Saratoga Fishing acquired the product from Madruga in 1974 as it did when Marco and Martinac installed the system, Marco and Martinac owe a duty to Saratoga Fishing regarding any design defect.

[4] In any case, the alterations made to the hydraulic system by Saratoga Fishing did not substantially alter the design of the system, which is what the district court found to be defective. The design of the system was the same on the day of the vessel's loss as it was when the SARATOGA left the shipyard.

B

Martinac and Marco argue that the district court erred in finding the design of the hydraulic system to be defective. They contend that the district court improperly applied a risk-utility test instead of a consumer or user expectations test to determine if the hydraulic system was defectively designed. Finally, Marco and Martinac argue, the district court misapplied the risk-utility test. We disagree with each of these contentions.

Admiralty courts use two methods to determine whether a product is defectively designed. The first method, drawn from Restatement section 402A comment i, provides that a product is defective if it is "dangerous to an extent beyond that which would be contemplated by the ordinary consumer who purchases it, with the ordinary knowledge common to the community as to its characteristics." This is the consumer expectations test. *See* Wonacott, *Shipbuilder Liability*, at 469; **Prosser & Keeton** § 99, at 698.

Although utilized by many courts, this test has come under criticism because of several shortcomings. First, it allows a manufacturer or seller to escape liability when the unreasonable danger is open and obvious. *See* **Prosser & Keeton** § 99, at 698-99; **M. Stuart Madden, Products Liability** § 6.7, at 213-14 (1988). Second, it is unpredictable in application. *See* **Prosser & Keeton** § 99, at 699. Because of the weaknesses of this test, some courts have sought an alternative way to determine whether a product was defectively designed.

A second test evolved from Judge Learned Hand's balancing test in a negligence case, *United States v. Carroll Towing Co.*, 159 F.2d 169, 173 (2d Cir. 1947). The risk-utility balancing test, in the context of a strict products liability action, weighs the utility of the product against the gravity of the danger. If, after considering the utility of the product, the economic and practical feasibility of alternative designs, and the gravity and likelihood of the potential harm, the factfinder determines that the risk outweighs the utility, the product is

deemed defective or unreasonably dangerous.[6] *See Pavlides v. Galveston Yacht Basin, Inc.*, 727 F.2d 330, 337 (5th Cir. 1984) (applying risk-utility test in admiralty case); *Borel v. Fibreboard Paper Prods. Corp.*, 493 F.2d 1076, 1078 (5th Cir. 1973) (nonadmiralty case), *cert. denied*, 419 U.S. 869 (1974); Wonacott, *Shipbuilder Liability*, at 469; **Prosser & Keeton** § 99, at 699-700.

[5] A recent law review article noted that "[a]dmiralty decisions reveal that no predictable fact pattern or particular liability theory will dictate application of any one test; so it is not believed possible to identify a consistently preferred admiralty standard." Wonacott, *Shipbuilder Liability*, at 471. The language of section 402A neither compels nor precludes the application of either test; it merely provides for an examination of whether a product is unreasonably dangerous.

We have not indicated which test or tests should be applied in admiralty cases in this circuit.[8] The district court rejected

[6]In a design defect case, the terms "defective condition" and "unreasonably dangerous" arguably share a common meaning. *See Hagans v. Oliver Mach. Co.*, 576 F.2d 97, 99 n.4 (5th Cir. 1978) (stating that "[a]s used in the Restatement" the two terms are synonymous); *see also* Carl T. Bogus, *Pistols, Politics & Products Liability*, 59 U. Cin. L. Rev. 1103, 1107-08 (1991) (arguing that in design defect cases, unreasonable danger is synonymous with defective condition); David P. Griffith, Note, *Products Liability—Negligence Presumed: An Evolution*, 67 Tex. L. Rev. 851, 859-60, 860 n.50 (1989) (citing sources supporting proposition that "defective" and "unreasonably dangerous" are synonymous and will lead to the same conclusion in design defect cases). Although we need not hold that the two terms will be synonymous in all cases, we use the terms interchangeably here. In other words, under either the consumer expectations test or the risk-utility test, a product that is deemed unreasonably dangerous will also be deemed to be in a defective condition. Conversely, a product in a defective condition must also be unreasonably dangerous.

[8]Marco and Martinac rely on *McCune v. F. Alioto Fish Co.*, 597 F.2d 1244 (9th Cir. 1979) and *Complaint of Diehl*, 610 F. Supp. 223 (Idaho 1985), to support their argument that only a consumer expectations test should be applied in admiralty. Neither case supports that proposition. *McCune* merely affirmed, without discussion, a district court's finding that a product was not defective. *Diehl*, which is a district court decision, did apply a consumer expectations test in the context of an admiralty case, but it did not discuss, and it certainly did not preclude, the applicability of other tests.

the pure application of the "so-called consumer's expectations" test in comments g and i of Restatement section 402A. Instead, the court applied the risk-utility test, citing the Fifth Circuit's decision in *Pavlides*. The district court proceeded to examine the risk and utility of the design along with the feasibility of alternative designs.

[6] We agree with the district court regarding the appropriateness of applying the risk-utility test in this case. If the consumer expectations test had been applied, the danger posed by the placement of the hoses of the hydraulic system in close proximity to the hot engine and turbocharger surfaces would likely be deemed open and obvious, especially to a purchaser or user of a fishing vessel. We are not satisfied with the possibility that a product with a design having high risk and limited utility, and a design that has other feasible alternatives, could be found not to be unreasonably dangerous or defective merely because a consumer, using the product in a foreseeable way, could recognize the danger.[7] As the district court correctly recognized, the risk-utility test provides a superior yardstick of whether a product is unreasonably dangerous or defective.

[7]Neither party argued that the product in this case was an unavoidably unsafe product. *See* Restatement § 402A cmt. k.

[7] We note that a preliminary draft of the Restatement (Third) of Torts by the reporters for the American Law Institute relies on a risk-utility analysis for deciding design defect cases. *See* Restatement (Third) of Torts: Products Liability § 2 (Tentative Draft No. 1, 1994). The tentative draft divides defective product cases into three categories: manufacturing defect cases, design defect cases, and inadequate warning cases. Proposed section 2(b) provides that "[a] product is defective in design when the foreseeable risks of harm posed by the product could have been reduced by the adoption of a reasonable alternative design by the seller . . . and the omission of the alternative design renders the product not reasonably safe." *Id.* § 2(b). Under the proposed Restatement, the consumer expectations test no longer "constitute[s] an independent standard for judging the defectiveness of product designs." *Id.* § 2(b) cmt. e. Instead, the focus is on the reasonableness of the design and the plaintiff's ability to prove that a reasonable alternative design would have reduced foreseeable risks of harm. *Id.* § 2(b) cmt. c. Although we need not, and do not, adopt the formulation of the Restatement (Third) at this time, it provides support for our holding that a focus on the design's benefits, risks, and feasible alternatives is a better approach to examining an alleged design defect. *See id.* § 2(b) cmt. c, reporters' note at 41 ("[s]cholarly commentary agrees overwhelmingly with . . . the risk-utility approach.").

[8] Our approval of an application of the risk-utility test in this case does not necessarily preclude future admiralty plaintiffs from showing a design defect using the consumer expectations test. In *Pan-Alaska*, we adopted the Restatement § 402A as the law of this circuit. That section includes comment i, which allows a consumer to show that a product was unreasonably dangerous in a way not contemplated by the consumer. Other jurisdictions permit a plaintiff to show a product design defect under either approach. *See, e.g., Barker*

v. Lull Engineering Co., 20 Cal.3d 413, 432, 573 P.2d 443 (1978); *Caterpillar Tractor Co. v. Beck*, 593 P.2d 871, 884 (Alaska 1979). Given our traditional discretion in admiralty, *see East River*, 476 U.S. at 871, we conclude that giving plaintiffs such a choice is appropriate.

Marco and Martinac next maintain that the district court improperly applied the risk-utility test because it failed to balance the various factors and failed to find that a feasible alternative design would have prevented the fire. Marco and Martinac also argue that the district court erred in finding the design unreasonably dangerous. We disagree.

[9] The district court examined the risk from the design of the hydraulic system, and found it extremely high. Saratoga Fishing presented evidence that hydraulic hoses can fail for a variety of reasons and that any failure under the currently designed system would lead to a serious fire. The district court considered the utility of the current design, but was persuaded that an alternative design, namely a metal shield placed to isolate the hot surfaces of the engine and turbocharger from the hydraulic hoses, would have led to less "harmful consequences."

[10] The district court did not rely on the mere technical possibility of a safer design. *See Glover v. BIC Corp.*, 987 F.2d 1410, 1422-23 (9th Cir.), *amended*, 6 F.3d 1318 (9th Cir. 1993). Rather, Saratoga Fishing presented evidence regarding specific feasible improvements in design. Indeed, Mr. Martinac himself testified that Martinac "now puts up a sheet metal barrier" in vessels. A barrier could have isolated the hydraulic hoses from the turbocharger and engine surfaces, while maintaining the utility of the system. Although the district court found that Marco and Martinac's failure to use such a shield at the time of construction did not violate any indus-

try rules or standards, it found the design unreasonably dangerous and defective because the design included a high risk of danger and there was a feasible alternative.

[11] Many qualified experts testified on both sides regarding the efficacy of the hydraulic system's design and the feasibility and safety of other designs. The parties disagree on whose experts and evidence deserve credence, as the experts disagreed on many critical issues, including whether the design was defective. We must accord due deference to the district court's consideration of the experts' testimony and the court's findings regarding that testimony. *Anderson v. City of Bessemer City*, 470 U.S. 564, 573-75 (1985) (citing Fed. R. Civ. P. 52(a)) ("[w]here there are two permissible views of the evidence, the factfinder's choice between them cannot be clearly erroneous."). The district court correctly applied the risk-utility test in finding the design of the hydraulic system defective. Its findings are not clearly erroneous.[8]

C

Marco and Martinac argue that the district court erred in finding that Saratoga Fishing's misuse and alteration of the hydraulic system was not a superseding cause of the accident and subsequent loss of the vessel. Again, we disagree.

[8]Although Saratoga Fishing contends that the district court also found Marco and Martinac negligent, the district court's findings and conclusions indicate that the only basis for its holding was strict products liability. The court's mention of negligence in a few places is not sufficient to establish a finding of liability. If the district court did intend to reach a negligence decision, it did not set forth negligence law or make findings regarding that law. Further, it did not address the critical issue in negligence, the fault of the defendant. It addressed only the unreasonably dangerous nature of the product. Thus, any conclusion of negligence is unsupported.

Any design defect must be shown to have contributed to, or caused the accident that led to the injury. *Matthews v. Hyster Co.*, 854 F.2d 1166, 1168 (9th Cir. 1988); **Prosser & Keeton** § 102, at 710-11 ("product defect under strict liability must be a proximate cause of claimant's injury"). Here, the presence of the hydraulic hoses near the hot engine and turbocharger surfaces without any effective shield was undoubtedly a proximate cause of and contributed to the fire that resulted in the vessel's loss. The district court found that this was the case, and this finding is not clearly erroneous.

Notwithstanding the existence of proximate cause, a manufacturer of a defective product can still be relieved of liability if some unforeseeable misuse or alteration occurred rising to the level of a superseding cause. **Prosser & Keeton** § 102, at 711. Marco and Martinac argue that such unforeseeable conduct occurred here.

They initially rely on a district court finding where the court purportedly stated that Saratoga Fishing's actions were a "precipitating cause" of the vessel's loss. Although the district court did make this finding, Marco and Martinac take it out of context. The court actually found that Saratoga Fishing's poor maintenance, misuse, and modifications to the hydraulic system "all contributed in some part to cause and bring about the catastrophic fire which ignited in the upper engine room . . . and was the precipitating cause of the vessel's loss . . . ." As this longer excerpt reveals, the court found that the fire was the precipitating cause of the loss. This is, of course, obvious. The court did not find that Saratoga Fishing's actions were a precipitating cause of the fire, rather it found that they were a contributing, or "substantial cause[ ]" of the fire.

[12] The district court did not find that Saratoga Fishing's

misuse and alteration of the hydraulic system amounted to a superseding cause of the accident. The district court could have, but did not, find Saratoga Fishing's misuse to be unforeseeable.[8] *Cf. Kay v. Cessna Aircraft Co.*, 548 F.2d 1370, 1372-73 (9th Cir. 1977) (plaintiff may recover if product is used in foreseeable, even if unintended use). The district court instead decided that hydraulic hose failure through either misuse, poor maintenance, or other conduct was foreseeable to Marco and Martinac, and that it would operate to reduce Saratoga Fishing's recovery but not to supersede Marco and Martinac's design defect as a proximate cause of the loss. This finding was not clearly erroneous.

[13] Marco and Martinac point to the alterations in the hydraulic system as examples that the system was modified substantially. The modifications, however, did not alter the design to the point where they superseded the design as a proximate cause of the fire.

D

Saratoga Fishing argues that the district court erred in reducing its award of damages by two-thirds based on the court's findings that it was also at fault for altering, misusing, failing to properly maintain, and ignoring the imminent failure of the hydraulic system. We agree with the district court.

[8]There was some controversy at trial over a water shield that was ostensibly installed over the turbocharger at the time the hydraulic system was installed on the SARATOGA. The district court was unable to determine whether this shield had been removed. It found however, that even if this shield had been in place, it would not have prevented the fire from igniting because it did not adequately cover the surfaces of the turbocharger and engine or isolate the hydraulic hoses from the surfaces. These findings are not clearly erroneous, and thus the presence or absence of the water shield does not affect Martinac and Marco's liability or affect whether Saratoga Fishing's actions constituted a superseding cause of the accident.

We have held that the concepts of "comparative fault (i.e., contributory negligence) . . . can be applied to the doctrine of strict products liability." *Pan-Alaska*, 565 F.2d at 1138. Under comparative fault principles, a party's blameworthy conduct that contributes to the proximate cause of the loss or injury will be compared to the defendant's liability and act to reduce the plaintiff's award of damages. *Id.* at 1139-40. As we stated: "It comes down to this: the defendant is strictly liable for the harm caused from his defective product, except that the award of damages shall be reduced in proportion to the plaintiff's contribution to his own loss or injury." *Id.* at 1139.

The district court found that Captain Vargas failed to properly maintain the hydraulic system. In an effort to increase the speed and power of the system, Vargas authorized enlarging the size of the seine, increasing the size of the power block, and increasing the velocity of the hydraulic flow and power to the machinery and equipment. This increased velocity raised the temperature of the hydraulic fluid and resulted in increased deterioration of the component parts of the hydraulic system, including the hydraulic hoses.

The district court also found that the engineers on board informed Captain Vargas that the hydraulic system was "overworked, wearing out and prone to an increasing number of failures." Vargas nonetheless continued to operate the system in excess of design pressures and temperatures and deferred remedial measures. Most significantly, the district court found that on January 16, the hydraulic hose that eventually failed was observed by the Chief Engineer and his assistant to be "leaking or weeping at the coupling."[9] Despite

[9]Although Chief Engineer Nielson testified that he did not consider the defective hose to be dangerous, the district court found that the engineer

being informed of the problem with the hose, Captain Vargas continued to operate the hydraulic system. The district court found that this created an "unreasonable risk that the hose would fail," causing hydraulic fluid to come in contact with the surface of the engine.

[14] The poor maintenance of the system, the modifications to the system, and the use of the system known to have a defective hose all contributed to the fire that caused the sinking of the vessel. The district court found that the conduct of those who manned the SARATOGA "border[ed] on irresponsible." The district judge is in the best position to weigh the evidence and apportion fault. *Alkmeon Naviera, S.A. v. M/V Marina L.*, 633 F.2d 789, 796 (9th Cir. 1980). The district court's determination is not clearly erroneous and the apportionment of two-thirds liability to Saratoga Fishing will not be disturbed.

Saratoga Fishing next argues that Marco and Martinac failed to establish the standard of care of a prudent tuna boat operator. We reject this argument. Marco and Martinac presented substantial evidence concerning proper maintenance and care of a fishing vessel's hydraulic system. That is more than sufficient to establish a standard of care.

IV

We next address the subject of damages. The district court awarded Saratoga Fishing $452,326, which sum equals one-third of the combined value of the following items: the tuna catch, net, skiff, fuel, assorted equipment, crew losses, rescue

must have been aware that it needed replacing and that the hydraulic system should not be operated. The district court also rejected Nielson's testimony that he was unaware of a risk of danger.

costs, and cash. The district court declined to award damages for the value of replacement parts and the vessel's hull. Marco, Martinac, and Saratoga Fishing raise various objections to the award. With one exception, we reject each of the arguments and agree with the district court's determinations.

[15] In *East River S.S. Corp v. Transamerica Delaval Inc.*, 476 U.S. 858 (1986), the Supreme Court recognized a significant limitation to its decision to adopt the law of strict products liability to admiralty. The Court drew a distinction between damage caused to the "product itself" and damage to a "person or other property." *Id.* at 870. When the product itself is damaged, the "resulting loss is purely economic" and losses such as "repair costs, decreased value, and lost profits . . . essentially [involve] the failure of the purchaser to receive the benefit of its bargain—traditionally the core concern of contract law." *Id.* At least in the commercial context, the Court stated that damage to a product should be sought by plaintiffs through a contract or warranty claim. A cause of action for damages in a products liability claim in admiralty is available only for an injury to persons or "other property." *Id.*

We have not yet had the opportunity to further define the contours of "other property." The Fifth Circuit has developed some principles in this area. In *Shipco 2295, Inc. v. Avondale Shipyards, Inc.*, 825 F.2d 925 (5th Cir. 1987), the Fifth Circuit was faced with the question whether the "product" consisted of a finished vessel or individual components that were included in the vessel. That court focused on the perspective of the buyer of the vessel, and held that the finished vessel that was the "object of the contract must be considered 'the product' rather than the individual components that make up the vessel[ ]." *Id.* at 928. The Fifth Circuit added that "the product in this context means the finished product bargained for by the buyer rather than components furnished by a supplier." *Id.* at 930.

A

We are faced here with a slightly different situation. The vessel that Martinac sold to Madruga constituted the "product" as far as Madruga was concerned. We must decide whether the "product" changed when Madruga added various components, including a skiff, seine and other miscellaneous parts, to the vessel and resold it to Saratoga Fishing.

We are guided by the policies set forth in *East River*, where the Court stated that the focus of the product should be on the failure of the purchaser to receive the benefit of its bargain. Warranty and contract law are appropriate for this type of situation. Here, the purchaser is Saratoga Fishing and the object of its bargain was the M/V SARATOGA with the components already installed. Saratoga Fishing purchased the vessel "as is." Madruga made no "warranty or representation of vessel condition."

The Fifth Circuit's decision in *Nicor Supply Ships Assoc. v. General Motors*, 876 F.2d 501 (5th Cir. 1989) is not in conflict with this principle. In that case, the vessel was sold only once. The buyer then time-chartered the vessel to a third-party, who installed equipment on the vessel. The court properly focused on the bargain between the buyer and shipbuilder to determine what was the product. *Id.* at 505-06. The equipment was deemed "other property."

East River provides a situation more similar to the one we confront here. In that case, the shipbuilder sold the vessel to a purchaser who subsequently executed an agreement with a bareboat charterer. The charterer took the vessel in an "as is" condition and assumed full responsibility for the vessel including maintenance, repair and insurance. 476 U.S. at 875. The Supreme Court focused on the terms of "the charterers'

agreements with the owners." *Id.* The Court also noted that the "contractual responsibilities thus were clearly laid out. There is no reason to extricate the parties from their bargain." *Id.* The contract being discussed is that between the first buyer and the bareboat charterer, who the Court treated as equivalent to a second buyer.

[16] Saratoga Fishing is the second buyer in this case. We must therefore focus on its agreement with Madruga. We see no reason to extricate Saratoga Fishing from its bargain. The parties chose not to include a seller's warranty, and we will not second guess their choice. The "product" in this case is the vessel that was delivered to Saratoga Fishing. Because it included the skiff, net, fuel, spare parts, and miscellaneous equipment, those items are part of the product and are not recoverable in a tort action as "other property."

It would indeed be anomalous for the shipbuilder's liability to increase every time the vessel was modified and resold. We agree with Marco and Martinac that such a result is inconsistent with *East River* and with the policies behind the application of products liability law to admiralty. The district court's award of damages to Saratoga Fishing for the skiff, net, fuel, spare parts, and miscellaneous equipment installed on the SARATOGA when it was sold to Saratoga Fishing is reversed.

Marco and Martinac next argue that an award of damages for the tuna catch was unjustified. They contend that the lost catch was a nonrecoverable pure economic loss under various theories: first, because the lost catch was a work in progress; second, because the lost catch was equivalent to damaged cargo; and third because it was similar to failed or damaged crops. We disagree.

[17] The tuna catch that was destroyed was different than

cargo because it was not being shipped from one site to another pursuant to a commercial agreement. It was new property on board the SARATOGA that belonged to the vessel's owner. The tuna was also not a work in progress as it had substantial value after being caught. The district court correctly reduced the value of the tuna by accounting for fuel costs and Panama Canal toll charges, and accurately computed the value of the tuna lying in the holds of the SARATOGA. Finally, the cases involving damaged crops are agricultural cases and are not helpful in the context of admiralty. We conclude that the tuna catch was not an economic loss, but was a loss of other property. The district court did not abuse its discretion in awarding damages for the tuna catch.

Marco and Martinac lastly contend that the district court erred in awarding Saratoga Fishing the value of Captain Vargas' lost currency because it was duplicative of sums awarded under the category of the lost crew property. The district court found that Vargas' testimony was "not effectively refuted" and was "credible." Marco and Martinac have shown insufficient evidence that the district court's findings were clearly erroneous. We will not disturb them.

B

Saratoga Fishing appeals the district court's refusal to award the value of replacement equipment installed in the vessel. It also argues that the district court erred in not permitting it to include the value of the vessel's hull in its damages sought from Marco.

[18] The district court concluded that replacement parts should not be recoverable as "other property" under *East River*. The court stated that permitting recovery would lead to

the absurd result that the shipbuilder's liability would grow as the performance of the product's relationship to the shipbuilder decreased. We agree. Because a product may have any number of components replaced with spare parts in the ordinary course of events, viewing these parts as "other property" would lead to absurd results. Such results would be contrary to the policies of *East River*, where the Supreme Court expressed its intention to exclude damages to the product itself from tort law and leave the injured party to remedies in the law of contract and warranty. 476 U.S. at 871-72; *see Exxon Shipping Co. v. Pacific Resources, Inc.*, 835 F. Supp. 1195, 1200 (D. Haw. 1993) (prohibiting recovery of cost of replacement parts in admiralty products liability action).

Saratoga Fishing lastly seeks damages from Marco (not Martinac) for the loss of the vessel itself. This argument is based on two propositions: first, that the approach to damages in *East River* should not apply to fishermen; and second, that for a component manufacturer such as Marco, the only "product" is its hydraulic system and that the vessel is "other property." Neither argument has merit.

Saratoga Fishing relies on footnote 5 in *East River*, in which the Supreme Court observed that it had at times applied a more protective approach in some admiralty contexts for fishermen, and that no fishermen were involved in that case. Even if that footnote reflected an exception to the rules set forth in *East River*, it is not applicable here. Saratoga Fishing is a company that owned an ocean-going tuna fishing vessel; there are no individual fishermen involved in this litigation. In any case, the only court that has considered the effect, if any, of the footnote, applied the *East River* damages rules without exception to a case involving plaintiffs who were fishermen. *McConnell v. Caterpillar Tractor Co.*, 646 F. Supp. 1520, 1525 (D.N.J. 1986).

Also without merit is Saratoga Fishing's argument that the

vessel should be deemed "other property" relative to Marco because Marco designed a component part of the vessel. The Fifth Circuit has rejected a similar claim. In *Shipco 2295, Inc. v. Avondale Shipyards, Inc.*, 825 F.2d 925, 928 (5th Cir. 1987), *cert. denied*, 485 U.S. 1007 (1988), the Fifth Circuit rejected a damages claim against the designer of a component part, observing that there is "no rational reason to give the buyer greater rights to recover economic losses for a defect in the product because the component is designed, constructed or furnished by someone other than the final manufacturer." *Id.* at 929.

[19] This rationale is sound. Saratoga Fishing bargained for a fishing vessel. That is the product. The hydraulic system is an integral part of the product. Seldom does one company design and build all component parts for an integrated product such as a fishing vessel. Indeed, Saratoga Fishing, as we noted above, bargained with Madruga, not Martinac, for the vessel, so Saratoga Fishing was one step removed from the initial purchase. Even if Madruga had sought recovery for the hull, however, it would make no difference. Permitting recovery from Marco for the vessel's hull would undermine the policy of *East River*—namely, that contract and warranty law should cover such losses, while tort law should be reserved for "other property."

C

Marco and Martinac argue that the district court erred in awarding prejudgment interest to Saratoga Fishing. They contend that Saratoga Fishing delayed filing a claim for almost two years after the vessel's loss and that Saratoga Fishing further delayed the litigation during a dispute over an attorney's conflict of interest.[11]

[11]Although Marco and Martinac initially objected to an award of prejudgment interest because of the high degree of Saratoga Fishing's comparative fault, they abandoned that ground on appeal.

"In admiralty, prejudgment interest must be granted unless peculiar circumstances justify its denial." *McKay v. Rockwell Int'l Corp.*, 704 F.2d 444, 463 (9th Cir. 1983), *cert. denied*, 464 U.S. 1043 (1984). The determination of whether peculiar circumstances exist is left to the district court's sound discretion. *Id.* at 464.

[20] Here, the district court concluded that this case was not "sufficiently peculiar or exceptional to justify departure from the general rule." Saratoga Fishing's claim was filed within the statute of limitations; thus, any delay was certainly not peculiar or unusual. The attorney conflict is also not an unusual occurrence. There is insufficient reason to disturb the district court's exercise of its sound discretion in awarding prejudgment interest.

Marco and Martinac also object to the district court's purported computation of postjudgment interest as inconsistent with the statutory mandate of 28 U.S.C. § 1961. Saratoga Fishing correctly points out, however, that the district court did not award postjudgment interest. It awarded additional prejudgment interest from the date of the damages findings and conclusions, June 1, 1993, until the date of final judgment, August 27, 1993. We find no error with the decision to award additional prejudgment interest. Of course, in light of our decision reversing part of the damages award, the district court should recompute the entire award of prejudgment interest on remand.

Finally, Saratoga Fishing is entitled to a further award of interest pursuant to 28 U.S.C. § 1961 from the date of entry of judgment until payment is made.

Appendix C

V

We are persuaded that the district court, having heard from all the experts and witnesses, did not, with the one aforementioned exception, err in deciding the issues of liability and damages. Marco and Martinac will pay their share because of their defectively designed hydraulic system, but Saratoga Fishing's award will be substantially reduced because of its failure to properly maintain and operate that system.

On remand the district court is directed to reconsider the amount of damages and interest and to enter judgment accordingly.

AFFIRMED in part, REVERSED in part and REMANDED. Each party shall bear its own costs.

APPENDIX D — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT FILED AUGUST 4, 1995

FOR PUBLICATION

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

SARATOGA FISHING CO., *Plaintiff-Appellee,* v. MARCO SEATTLE INC., *Defendant-Appellant,* v. J.M. MARTINAC & CO.; CATERPILLAR TRACTOR CO.; SOUTHWEST MARINE HARDWARE, INC., *Defendants.*	No. 93-56344 D.C. No. CV-87-01691-JMF OPINION
SARATOGA FISHING CO., *Plaintiff-Appellant,* v. MARCO SEATTLE INC.; SOUTHWEST MARINE HARDWARE, INC.; CATERPILLAR TRACTOR CO.; J.M. MARTINAC & CO., *Defendants-Appellees.*	No. 93-56368 D.C. No. CV-87-01691-JMF

Appendix D

SARATOGA FISHING CO.,
Plaintiff-Appellee,
v.
J.M. MARTINAC & CO.,
Defendant-Appellant.

No. 93-56501
D.C. No.
CV-87-01691-JMF

Appeals from the United States District Court
for the Southern District of California
James M. Fitzgerald, Chief Judge, Presiding

Argued and Submitted
February 8, 1995—Pasadena, California

Filed April 25, 1995

Before: Robert R. Beezer and John T. Noonan, Jr., Circuit Judges, and David Alan Ezra, District Judge.*

Opinion by Judge Beezer

SUMMARY

Admiralty & Marine/Torts/Litigation & Procedure

The court of appeals affirmed a judgment of the district court. The court held that in an admiralty suit by a shipowner against the vessel's builder and a component manufacturer for product liability based on design defect, the district court may apply either risk-utility or consumer expectation analysis.

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*The Honorable David Alan Ezra, United States District Judge for the District of Hawaii, sitting by designation.

Appendix D

An engine room fire led to the sinking of M/V *Saratoga* without injury to any of her crew. Appellee Saratoga Fishing Co., the vessel's owner, sued appellants J.M. Martinac & Co., the shipbuilder, and Marco Seattle, the manufacturer of the shipboard hydraulic system. The complaint alleged that the fire was caused by defects in the design of the hydraulic system, which failed and spilled inflammable fluid on the hot surface of the *Saratoga*'s engine. Saratoga proceeded on theories of strict liability, negligence, and failure to warn.

The evidence showed that the ship's captain ignored signs and warnings of an overloaded hydraulic system before the fire, and that the owner had modified various systems of the ship to increase speed and power. The resultant increased velocity of hydraulic fluid to machinery and equipment increased deterioration of component parts, and eventually precipitated the eruption of a pressure hose near the hot engine.

Marco and Martinac argued that the vessel's design was not defective, that Saratoga had failed to maintain the fire suppression system or the hydraulic hoses, and had substantially altered and misused the hydraulic system.

Applying risk-utility analysis, the district court concluded that the hydraulic system was defectively designed despite its conformity to established marine practices, and that Marco and Martinac were strictly liable for the *Saratoga* 's loss. The court found that the risk from the system design was extremely high, that a feasible alternative design (shield between hose and engine) would have led to less serious consequences, and that hydraulic hose failure was foreseeable to Marco and Martinac.

The court also determined that Saratoga was at fault due to its poor maintenance and overuse of the hydraulic system, and its failure to act on signs of imminent failure. Accordingly, the court reduced Saratoga's award by two thirds. The award of damages did not include replacement parts or the hull, the latter excluded on the ground that it was not recoverable in an admiralty products liability action.

On appeal, Marco and Martinac also contended that they owed no duty to Saratoga because it was a sophisticated commercial buyer, and that Saratoga failed to establish that the hydraulic system was free of substantial change from its condition when it left the builder's yard.

[1] A commercial seller of a maritime product may be strictly liable to a sophisticated commercial buyer. Many maritime transactions occur between commercial sellers and sophisticated buyers; the position advocated by Marco and Martinac would tend to eliminate what has already been accepted: strict products liability is part of the general maritime law.

[2] Any misuse or fault by the user or consumer can and did reduce the plaintiff's recovery, and may even relieve the manufacturer or seller from liability. But the duty to the consumer or user exists if the product was in a defective condition at the time the consumer or user obtained the product. [3] In any case, the alterations to the hydraulic system by Saratoga did not substantially alter the design of the system, which is what the district court found to be defective.

[4] The district court was correct regarding the appropriateness of the risk-utility test. It is not satisfactory that a product with a high-risk design defect and limited utility that has feasible alternatives could be found not unreasonably dangerous or defective merely because a consumer using it in a foreseeable way could recognize the danger. [5] A focus on the design's benefits, risks, and feasible alternatives is a better approach to examining an alleged design defect.

[6] Approval of an application of the risk-utility test in this case did not preclude future admiralty plaintiffs from showing a design defect using the consumer expectations test. Giving plaintiffs a choice is appropriate.

[7] The district court's conclusion that the failure of the hydraulic hose through misuse, poor maintenance, or other conduct was foreseeable to Marco and Martinac was not clearly erroneous. [8] The modifications did not alter the design to the point where they superseded the design as a proximate cause of the fire.

[9] Concepts of comparative fault can be applied to the doctrine of strict products liability. [10] The poor maintenance and use of and alterations to the hydraulic system contributed to the fire that led to the sinking of *Saratoga*. The district court's apportionment of fault was not clearly erroneous.

[11] A cause of action for damages in a products liability claim in admiralty is available only for injury to persons and "other property." [12] A products liability plaintiff is not able to recover damages for economic losses resulting from the loss of the vessel, but can recover them for items added to the vessel by its user.

[13] Although the components added by the owner were integral to the operation of the ship, they were not part of the vessel that Martinac sold to the original owner. The items for

which the district court awarded damages were different from the component parts that were part of the vessel when it was delivered. [14] The tuna catch that was destroyed was not cargo because it was not being shipped from one point to another pursuant to a commercial agreement; it was new property that belonged to the vessel's owner. It was not a work in progress because it had substantial value after being caught. Nor was it like damaged crops in agricultural cases because the context was admiralty.

[15] Because a product may have any number of components replaced with spare parts in the ordinary course of events, viewing them as "other property" would lead to absurd results, and contravene the policy excluding damage to the product itself to tort law and leave the injured party to contract and warranty remedies. [16] Permitting recovery from Marco for the hull would undermine the same policy.

COUNSEL

Daniel B. MacLeod, Alford & MacLeod, San Diego, California, for defendant-appellant-cross-appellee Marco Seattle, Inc. Duncan B. Koler, Walton, Ottesen, Meads & Koler, San Diego, California, for defendant-appellant-cross-appellee J.M. Martinac & Company.

Keith Zakarin, Pillsbury, Madison & Sutro, San Diego, California, for plaintiff-appellee-cross-appellant Saratoga Fishing Company.

OPINION

BEEZER, Circuit Judge:

This products liability action in admiralty arose following an engine room fire that caused the flooding and sinking of the fishing vessel M/V SARATOGA. The district court concluded that J.M. Martinac & Company ("Martinac"), the shipbuilder, and Marco Seattle, Inc. ("Marco"), the designer of the vessel's hydraulic system, were strictly liable to Saratoga Fishing Company ("Saratoga Fishing"), the vessel owner, for damages to "other property" on the vessel because the fire and subsequent loss resulted from a defectively designed hydraulic system. The district court reduced the damages award by two-thirds, however, because of Saratoga Fishing's comparative fault in maintaining and operating that system. Both sides appeal the district court's determinations on liability and damages.[1]

We have jurisdiction over these timely appeals pursuant to 28 U.S.C. § 1291. Because we agree with the district court's resolution of this action, we affirm.

I

We retrace the fateful path of the fishing vessel M/V SARATOGA ("SARATOGA"). The vessel was designed and built in 1971 by Martinac in its Tacoma, Washington shipyards for Joseph McDruga. During the construction process, Martinac, after consulting with McDruga, contracted with Marco to design a hydraulic system. The system was installed by Martinac and inspected by Marco.

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[1]Two other defendants, Caterpillar Tractor Company and Southwest Marine Hardware, Inc., are not parties to this appeal.

Appendix D

The SARATOGA's hydraulic system included pumps, pump drives, control valves, hoses and pressure gauges all connected to a 190-horsepower Caterpillar D333 engine and turbocharger. The system operated machinery and equipment such as a power block, a boom and winches, which were necessary to use the seine (net) for tuna fishing operations. Hydraulic fluid was pumped through the system to operate the deck machinery. The fluid exited the pumps through five rubber hoses attached to the pump drive by metal couplings. The hoses rose vertically from the pump to the overhead, passing near the engine and turbocharger.

The completed vessel was launched in 1972. Its captain, Manuel Vargas, took the vessel from San Diego, where it had undergone various sea trials, to Panama where she was outfitted with a seine and other fishing equipment. The SARATOGA then commenced tuna fishing operations.

In 1974, the Manuel S. Vargas, Jr. Corporation, which was principally owned by Vargas and later changed its name to Saratoga Fishing, purchased the SARATOGA from McDruga. At the time of sale, the vessel was equipped with five speedboats, a purse skiff, a seine, and various electronic equipment. Vargas continued to serve as captain until 1979.

When Vargas returned to the SARATOGA as captain in 1984, the condition of the vessel had deteriorated. While overseeing a refurbishing of the vessel, Vargas ordered a series of modifications to various machinery and equipment: the size of the seine was increased; a larger boom was installed; a larger power block was installed; larger cartridges were installed in the pumps; and a 100-horsepower electric drive and pump were installed to increase power to the hydraulic system above that of the original equipment.

Appendix D

A new Chief Engineer joined the vessel in 1984. Wesley Ogilvie noticed on his first fishing trip that the hydraulic system was experiencing failures, such as leaking valves and breaking hoses. Nevertheless, Captain Vargas continued to seek increased power to the hydraulic system to quicken the speed at which the seine could be pursed. Assistant Engineer Lewis Jorge joined the crew in 1985, and observed worn out pump cartridges and an overloaded hydraulic system. In late 1985, Ogilvie was replaced as Chief Engineer by Mark Nielson, who noticed more problems with the hydraulic system. Hydraulic hoses needed replacement, winches were leaking hydraulic fluid, and the temperature of the hydraulic fluid was abnormally high.

Various repair work was completed on the SARATOGA when she docked in Panama late in 1985, including the replacement of seals in the hydraulic system and pump cartridges. Workers also repaired damage to the turbocharger on the main engine. On January 8, 1986, the SARATOGA departed Panama to fish for tuna near the Gallapagos Islands in the Pacific Ocean.

On the afternoon of January 16, Chief Engineer Nielson observed one hydraulic hose seeping hydraulic fluid at the coupling attaching the hose to the pump. Although Captain Vargas arranged to rendezvous with another vessel to obtain a necessary tool to manufacture a replacement hose, Vargas did not shut down the hydraulic system. Instead, Vargas utilized the system to catch more tuna late that afternoon.

A short time later, Lewis Jorge entered the engine room and observed that a hydraulic hose was "pulsating." As Jorge watched, the hose pulled out of its coupling and hydraulic fluid sprayed up from the coupling and fell back onto the hot surface of the turbocharger. The fluid ignited causing an immediate conflagration in the engine room. Jorge and Niel-

son attempted to extinguish the fire, but their efforts were unsuccessful.

The fire quickly spread throughout the SARATOGA, and Captain Vargas ordered the crew to abandon ship. The crew left in a skiff, and were soon rescued by another vessel. No crew member suffered serious injury. Unfortunately, the SARATOGA sank.[2]

Property losses included, in addition to the loss of the vessel, all of the fishing equipment, fuel, a substantial tuna catch stored in the vessel, crew members' personal property losses, and $16,000 in cash that Captain Vargas had placed in the vessel's safe.

Saratoga Fishing brought the instant lawsuit in district court against Martinac and Marco within the court's admiralty jurisdiction seeking recovery for property losses. *See* 28 U.S.C. § 1333. The court conducted a 14-day trial in which it heard testimony from a variety of expert witnesses and considered a substantial amount of evidence.

At trial, Saratoga Fishing argued that the hydraulic system was defectively designed. It sought recovery under theories of strict liability, negligence, and failure to warn.

Saratoga Fishing offered, among other witnesses, the expert testimony of David Saveker, a naval architect. Saveker testi-

[2]Although the district court found that the cause of the SARATOGA's sinking was the flooding that occurred as a consequence of the fire, it was unable to determine exactly how and why the flooding occurred. The district court determined that resolving that question was not necessary to its disposition. We agree.

fied that the Marco hydraulic drive system incorporated an unsafe design. The hydraulic hoses were, in Saveker's opinion, located too close to the hot surfaces of the engine and turbocharger. As hydraulic hoses and couplings are prone to fail for a variety of reasons, Saveker noted, the designer of the hydraulic system should have taken preventive measures such as relocating the hoses elsewhere, installing an electric instead of a diesel motor to reduce the risk of a fire developing from leaking hydraulic fluid, or isolating the hoses from the engine and turbocharger by the use of shielding. Such shielding would have "screen[ed] out a large percentage of the probability of an immediate torch" from the leaking hydraulic fluid. Saveker testified that the system was "a bad accident waiting to happen."

Marco and Martinac argued that the vessel's design was not defective, that Saratoga Fishing had failed to maintain the fire suppression system or the hydraulic hoses, and that Saratoga Fishing had substantially altered and misused the hydraulic system.

Larry Grief, a marine architect, testified as an expert witness for Marco and Martinac. He stated that the hydraulic system on board the SARATOGA met well-established marine practice and was similar to those on almost every vessel he had been aboard. The hydraulic hoses, Grief noted, were designed with a safety margin of 6 to 1 over standard operating pressures. In Grief's opinion, the hydraulic system was not operating properly because of the modifications made by Saratoga Fishing. The addition of a 100-horsepower electric drive caused the hydraulic fluid to pass through the system at a higher velocity, leading to a corresponding increase in the temperature of the hydraulic fluid, which in turn caused rapid deterioration. Furthermore, the larger equipment (seine,

boom, and power block) installed by Saratoga Fishing required more hydraulic power, but the installation was not accompanied by any modifications in the hydraulic hoses.

The district court concluded that Marco and Martinac were strictly liable for the loss of the SARATOGA. The court found that the hydraulic system was defectively designed despite the fact that it met established marine practices. The placement of the hydraulic hoses in close proximity to the engine and turbocharger presented a known serious risk of fire and, the district court found, feasible design changes, such as the placement of a shield or barrier to isolate the hydraulic hoses from the engine and turbocharger, would have reduced the risk. The modifications made by Saratoga Fishing did not alter the chain of causation because they did not affect the design.

The court also found, however, that Saratoga Fishing was at fault due to its poor maintenance of the hydraulic system, its overuse of the system, and its failure to recognize the signs of imminent failure of the system. Saratoga Fishing's comparative fault reduced its recovery by two-thirds.

In a later ruling, the district court awarded damages to Saratoga Fishing in the amount of $452,326, one-third of the sum it determined to be Saratoga Fishing's total damages. The award included losses of the tuna catch, seine, skiff, fuel, equipment, the crews' personal losses, the cost of the rescue, and Captain Vargas' cash.

Not included in the award was the loss of any replacement parts that Saratoga Fishing installed on the vessel. The award also did not include the loss of the vessel's hull, which the trial court had decided pretrial was not recoverable from either defendant in an admiralty products liability action.

The court awarded prejudgment interest, which raised the total award to Saratoga Fishing to $734,940.38. Finally, the court awarded additional interest to Saratoga Fishing until the date of the final judgment at the rate of $153.09 per day.

II

We review the admiralty trial court's findings of fact for clear error, and its conclusions of law *de novo*. *Havens v. F/T Polar Mist*, 996 F.2d 215, 217 (9th Cir. 1993). The existence and extent of a duty are questions of law reviewed *de novo*, while proximate cause and whether such a duty has been breached are questions of fact reviewed for clear error. *Martinez v. Korea Shipping Corp.*, 903 F.2d 606, 609 (9th Cir. 1990).

We review *de novo* the legal conclusion that damages are available. *United States v. Timberland Paving & Constr. Co.*, 745 F.2d 595, 599 (9th Cir. 1984) ("[w]e review questions of law de novo"). Finally, we review for clear error a trial court's factual findings in support of an award for damages. *Bergen v. F/V St. Patrick*, 816 F.2d 1345, 1347 (9th Cir. 1987), *cert. denied*, 493 U.S. 871 (1989).

III

Saratoga's claims fall within the admiralty jurisdiction, as they arose on the high seas. 28 U.S.C. § 1333; *see Jerome B. Grubart, Inc. v. Great Lakes Dredge & Dock Co.*, 63 U.S.L.W. 4154, 4155-56 (U.S. Feb. 22, 1995). We apply, as the district court did, substantive admiralty law, which, absent a federal statute, is the general maritime law. *East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858, 864 (1986). The law of products liability, including strict liability,

is recognized as part of the general maritime law. *Id.* at 865; *Pan-Alaska Fisheries, Inc. v. Marine Constr. & Design Co.*, 565 F.2d 1129, 1135 (9th Cir. 1977).

In holding that a strict products liability action would lie in admiralty, we adopted the Restatement (Second) of Torts § 402A (1965) as "the law of products liability in this circuit" because it was "the best and most widely-accepted expression of the theory of strict products liability." *Pan-Alaska*, 565 F.2d at 1135. Section 402A provides as follows:

> (1) One who sells any product in a defective condition unreasonably dangerous to the user or consumer or to his property is subject to liability for physical harm thereby caused to the ultimate user or consumer, or to his property, if
>
> (a) the seller is engaged in the business of selling such a product, and
>
> (b) it is expected to and does reach the user or consumer without substantial change in the condition in which it is sold.
>
> (2) The rule stated in Subsection (1) applies although
>
> (a) the seller has exercised all possible care in the preparation and sale of his product, and
>
> (b) the user or consumer has not bought the product from or entered into any contractual relation with the seller.

Under the doctrine of strict products liability, manufacturers and sellers of products are held liable because society considers them better able than individuals to bear the costs of injuries and damage resulting from defective products. *See* **W. Page Keeton et al., Prosser and Keeton on Torts** § 98, at 692-93 (5th ed. 1984) [hereinafter **Prosser & Keeton**] (manufacturers and sellers "have the capacity to distribute the losses of the few among the many who purchase the products"); *Greenman v. Yuba Power Prods., Inc.*, 59 Cal.2d 57, 377 P.2d 897 (1963); **Thomas J. Schoenbaum, Admiralty and Maritime Law** § 5-6, at 177 (1994) (policies underlying strict liability apply in admiralty).

A

Martinac and Marco argue, based on two theories, that the district court erred in concluding that they owed any duty to Saratoga Fishing. They contend first that Saratoga Fishing was a sophisticated commercial buyer and that imposition of a strict products liability duty in this context is unwarranted. Next, Martinac and Marco argue that Saratoga Fishing failed to establish that the vessel, specifically the hydraulic system, was without substantial change. Thus, they contend that under Restatement section 402A(1)(b), they had no duty to protect Saratoga Fishing from a defective condition unreasonably dangerous to it.[3]

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[3]Marco and Martinac also argue that the trial court erroneously found that they had a duty to provide a "safe vessel." We agree that their duty was to provide a vessel that was not unreasonably dangerous to the user. In our judgment, however, the district court's choice of words in one finding does not undermine the propriety of its analysis of the appropriate nature of Marco and Martinac's duty.

Marco and Martinac raise interesting policy arguments for why commercial sellers should not owe a strict products liability duty to sophisticated commercial buyers of products such as fishing vessels. Many of the concerns animating strict products liability, including the ability of manufacturers and sellers to better absorb the costs of defective products, do not necessarily support strict products liability in this context. Indeed, private insurance on the part of the vessel's owner would, it is argued, provide a more effective economic allocation of risk. We have also recognized that section 402A of the Restatement "should be applied only when the purposes it seeks to serve dictate its application." *McKay v. Rockwell Int'l Corp.*, 704 F.2d 444, 447 (9th Cir. 1983), *cert. denied*, 464 U.S. 1043 (1984).

[1] The question is not, however, an open one in this circuit. We have held a commercial seller of a maritime product strictly liable under Restatement section 402A in a factually similar case involving a presumably sophisticated commercial buyer. *Pan-Alaska*, 565 F.2d at 1134-37; *see also East River*, 476 U.S. 864-66, 871 (discussing application of strict products liability to "manufacturer in a commercial relationship"). Although we have not specifically considered the policy arguments raised here, we have yet to create an exception to strict products liability for certain sellers based on the commercial nature of the sale.[4] *See* Paul N. Wonacott, *Products Liabilities of Shipbuilders and Repairers*, 62 Tulane L. Rev. 465, 469 (1988) (liability for a defective product under section 402A

[4]In *McKay*, 704 F.2d at 447 n.4, we recognized those limited circumstances when strict products liability does not apply. They include unavoidably unsafe products, used products and services. We also added to that list in *McKay* that only in limited circumstances should a manufacturer be held strictly liable in tort for injuries to a service member in active duty caused by a design defect in military equipment. *Id.* at 447-48.

attaches in admiralty regardless whether "the accident-causing product is a structure uniquely designed to a particular owner's specifications"). Because many maritime transactions occur between commercial sellers and sophisticated buyers, the position advocated by Marco and Martinac would tend to eliminate what we have already accepted—that strict products liability is a part of the general maritime law.

Marco and Martinac's other argument regarding strict products liability duty is also unavailing. They misperceive the meaning of "substantial change" as defined by section 402A(1)(b). The Restatement section 402A provides that the product must "reach the user or consumer without substantial change in the condition in which it is sold." Thus, if a manufacturer's product is altered by a seller or other intermediary, the manufacturer might be immune from strict liability. *See* Restatement § 402A cmt. p. Once the produet has reached the "user or consumer," however, that element has been satisfied. *See Emerson G.M. Diesel, Inc. v. Alaskan Enter.*, 732 F.2d 1468, 1475 (9th Cir. 1984) (product must not be "altered or changed when it reached the consumer"), *overruled in part on other grounds by East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858 (1986).

[2] Any misuse or fault by the user or consumer could and indeed, in this case, did reduce the plaintiff's recovery. Restatement § 402A cmt. n; *Pan-Alaska*, 565 F.2d at 1138 (comparative fault concepts can be applied to strict products liability). Whether the plaintiff misused the product, or significantly altered the product so as to become an intervening, superseding proximate cause of the resulting loss may even relieve the manufacturer or seller from liability altogether, but that misuse or alteration does not relate to whether the manufacturer or seller had a duty to the consumer or user. The duty

exists if the product was in a defective condition at the time the consumer or user obtained the product. Because the hydraulic system retained the same design when Saratoga Fishing acquired the product from McDruga in 1974 as it did when Marco and Martinac installed the system, Marco and Martinac owe a duty to Saratoga Fishing regarding any design defect.

[3] In any case, the alterations made to the hydraulic system by Saratoga Fishing did not substantially alter the design of the system, which is what the district court found to be defective. The design of the system was the same on the day of the vessel's loss as it was when the SARATOGA left the shipyard.

B

Martinac and Marco argue that the district court erred in finding the design of the hydraulic system to be defective. They contend that the district court improperly applied a risk-utility test instead of a consumer or user expectations test to determine if the hydraulic system was defectively designed. Finally, Marco and Martinac argue, the district court misapplied the risk-utility test. We disagree with each of these contentions.

Admiralty courts use two methods to determine whether a product is defectively designed. The first method, drawn from Restatement section 402A comment i, provides that a product is defective if it is "dangerous to an extent beyond that which would be contemplated by the ordinary consumer who purchases it, with the ordinary knowledge common to the community as to its characteristics." This is the consumer expectations test. *See* Wonacott, *Shipbuilder Liability*, at 469; **Prosser & Keeton** § 99, at 698.

Although utilized by many courts, this test has come under criticism because of several shortcomings. First, it allows a manufacturer or seller to escape liability when the unreasonable danger is open and obvious. *See* **Prosser & Keeton** § 99, at 698-99; **M. Stuart Madden, Products Liability** § 6.7, at 213-14 (1988). Second, it is unpredictable in application. *See* **Prosser & Keeton** § 99, at 699. Because of the weaknesses of this test, some courts have sought an alternative way to determine whether a product was defectively designed.

A second test evolved from Judge Learned Hand's balancing test in a negligence case, *United States v. Carroll Towing Co.*, 159 F.2d 169, 173 (2d Cir. 1947). The risk-utility balancing test, in the context of a strict products liability action, weighs the utility of the product against the gravity of the danger. If, after considering the utility of the product, the economic and practical feasibility of alternative designs, and the gravity and likelihood of the potential harm, the factfinder determines that the risk outweighs the utility, the product is deemed defective or unreasonably dangerous.[8] *See Pavlides v.*

[8]In a design defect case, the terms "defective condition" and "unreasonably dangerous" arguably share a common meaning. *See Hagans v. Oliver Mach. Co.*, 576 F.2d 97, 99 n.4 (5th Cir. 1978) (stating that "[a]s used in the Restatement" the two terms are synonymous); *see also* Carl T. Bogus, *Pistols, Politics & Products Liability*, 59 U. Cin. L. Rev. 1103, 1107-08 (1991) (arguing that in design defect cases, unreasonable danger is synonymous with defective condition); David P. Griffith, Note, *Products Liability—Negligence Presumed: An Evolution*, 67 Tex. L. Rev. 851, 859-60, 860 n.50 (1989) (citing sources supporting proposition that "defective" and "unreasonably dangerous" are synonymous and will lead to the same conclusion in design defect cases). Although we need not hold that the two terms will be synonymous in all cases, we use the terms interchangeably here. In other words, under either the consumer expectations test or the risk-utility test, a product that is deemed unreasonably dangerous will also be deemed to be in a defective condition. Conversely, a product in a defective condition must also be unreasonably dangerous.

Galveston Yacht Basin, Inc., 727 F.2d 330, 337 (5th Cir. 1984) (applying risk-utility test in admiralty case); *Borel v. Fibreboard Paper Prods. Corp.*, 493 F.2d 1076, 1078 (5th Cir. 1973) (nonadmiralty case), *cert. denied*, 419 U.S. 869 (1974); Wonacott, *Shipbuilder Liability*, at 469; **Prosser & Keeton** § 99, at 699-700.

A recent law review article noted that "[a]dmiralty decisions reveal that no predictable fact pattern or particular liability theory will dictate application of any one test; so it is not believed possible to identify a consistently preferred admiralty standard." Wonacott, *Shipbuilder Liability*, at 471. The language of section 402A neither compels nor precludes the application of either test; it merely provides for an examination of whether a product is unreasonably dangerous.

We have not indicated which test or tests should be applied in admiralty cases in this circuit.[6] The district court rejected the pure application of the "so-called consumer's expectations" test in comments g and i of Restatement section 402A. Instead, the court applied the risk-utility test, citing the Fifth Circuit's decision in *Pavlides*. The district court proceeded to examine the risk and utility of the design along with the feasibility of alternative designs.

[6]Marco and Martinac rely on *McCune v. F. Alioto Fish Co.*, 597 F.2d 1244 (9th Cir. 1979) and *Complaint of Diehl*, 610 F. Supp. 223 (Idaho 1985), to support their argument that only a consumer expectations test should be applied in admiralty. Neither case supports that proposition. *McCune* merely affirmed, without discussion, a district court's finding that a product was not defective. *Diehl*, which is a district court decision, did apply a consumer expectations test in the context of an admiralty case, but it did not discuss, and it certainly did not preclude, the applicability of other tests.

[4] We agree with the district court regarding the appropriateness of applying the risk-utility test in this case. If the consumer expectations test had been applied, the danger posed by the placement of the hoses of the hydraulic system in close proximity to the hot engine and turbocharger surfaces would likely be deemed open and obvious, especially to a purchaser or user of a fishing vessel. We are not satisfied with the possibility that a product with a design having high risk and limited utility, and a design that has other feasible alternatives, could be found not to be unreasonably dangerous or defective merely because a consumer, using the product in a foreseeable way, could recognize the danger.[7] As the district court correctly recognized, the risk-utility test provides a superior yardstick of whether a product is unreasonably dangerous or defective.

[5] We note that a preliminary draft of the Restatement (Third) of Torts by the reporters for the American Law Institute relies on a risk-utility analysis for deciding design defect cases. *See* Restatement (Third) of Torts: Products Liability § 2 (Tentative Draft No. 1, 1994). The tentative draft divides defective product cases into three categories: manufacturing defect cases, design defect cases, and inadequate warning cases. Proposed section 2(b) provides that "[a] product is defective in design when the foreseeable risks of harm posed by the product could have been reduced by the adoption of a reasonable alternative design by the seller . . . and the omission of the alternative design renders the product not reasonably safe." *Id.* § 2(b). Under the proposed Restatement, the consumer expectations test no longer "constitute[s] an independent standard for judging the defectiveness of product designs." *Id.* § 2(b) cmt. e. Instead, the focus is on the reason-

[7]Neither party argued that the product in this case was an unavoidably unsafe product. *See* Restatement § 402A cmt. k.

ableness of the design and the plaintiff's ability to prove that a reasonable alternative design would have reduced foreseeable risks of harm. *Id.* § 2(b) cmt. c. Although we need not, and do not, adopt the formulation of the Restatement (Third) at this time, it provides support for our holding that a focus on the design's benefits, risks, and feasible alternatives is a better approach to examining an alleged design defect. *See id.* § 2(b) cmt. c, reporters' note at 41 ("[s]cholarly commentary agrees overwhelmingly with . . . the risk-utility approach.").

[6] Our approval of an application of the risk-utility test in this case does not necessarily preclude future admiralty plaintiffs from showing a design defect using the consumer expectations test. In *Pan-Alaska*, we adopted the Restatement § 402A as the law of this circuit. That section includes comment i, which allows a consumer to show that a product was unreasonably dangerous in a way not contemplated by the consumer. Other jurisdictions permit a plaintiff to show a product design defect under either approach. *See, e.g., Barker v. Lull Engineering Co.*, 20 Cal.3d 413, 432, 573 P.2d 443 (1978); *Caterpillar Tractor Co. v. Beck*, 593 P.2d 871, 884 (Alaska 1979). Given our traditional discretion in admiralty, *see East River*, 476 U.S. at 871, we conclude that giving plaintiffs such a choice is appropriate.

Marco and Martinac next maintain that the district court improperly applied the risk-utility test because it failed to balance the various factors and failed to find that a feasible alternative design would have prevented the fire. Marco and Martinac also argue that the district court erred in finding the design unreasonably dangerous. We disagree.

The district court examined the risk from the design of the hydraulic system, and found it extremely high. Saratoga Fishing presented evidence that hydraulic hoses can fail for a variety of reasons and that any failure under the currently designed system would lead to a serious fire. The district court considered the utility of the current design, but was persuaded that an alternative design, namely a metal shield placed to isolate the hot surfaces of the engine and turbocharger from the hydraulic hoses, would have led to less "harmful consequences."

The district court did not rely on the mere technical possibility of a safer design. *See Glover v. BIC Corp.*, 987 F.2d 1410, 1422-23 (9th Cir.), *amended*, 6 F.3d 1318 (9th Cir. 1993). Rather, Saratoga Fishing presented evidence regarding specific feasible improvements in design. Indeed, Mr. Martinac himself testified that Martinac "now puts up a sheet metal barrier" in vessels. A barrier could have isolated the hydraulic hoses from the turbocharger and engine surfaces, while maintaining the utility of the system. Although the district court found that Marco and Martinac's failure to use such a shield at the time of construction did not violate any industry rules or standards, it found the design unreasonably dangerous and defective because the design included a high risk of danger and there was a feasible alternative.

Many qualified experts testified on both sides regarding the efficacy of the hydraulic system's design and the feasibility and safety of other designs. The parties disagree on whose experts and evidence deserve credence, as the experts disagreed on many critical issues, including whether the design was defective. We must accord due deference to the district court's consideration of the experts' testimony and the court's findings regarding that testimony. *Anderson v. City of Bessemer City*, 470 U.S. 564, 573-75 (1985) (citing Fed. R. Civ. P.

52(a)) ("[w]here there are two permissible views of the evidence, the factfinder's choice between them cannot be clearly erroneous."). The district court correctly applied the risk-utility test in finding the design of the hydraulic system defective. Its findings are not clearly erroneous.[8]

C

Marco and Martinac argue that the district court erred in finding that Saratoga Fishing's misuse and alteration of the hydraulic system was not a superseding cause of the accident and subsequent loss of the vessel. Again, we disagree.

Any design defect must be shown to have contributed to, or caused the accident that led to the injury. *Matthews v. Hyster Co.*, 854 F.2d 1166, 1168 (9th Cir. 1988); **Prosser & Keeton** § 102, at 710-11 ("product defect under strict liability must be a proximate cause of claimant's injury"). Here, the presence of the hydraulic hoses near the hot engine and turbocharger surfaces without any effective shield was undoubtedly a proximate cause of and contributed to the fire that resulted in the vessel's loss. The district court found that this was the case, and this finding is not clearly erroneous.

[8]Although Saratoga Fishing contends that the district court also found Marco and Martinac negligent, the district court's findings and conclusions indicate that the only basis for its holding was strict products liability. The court's mention of negligence in a few places is not sufficient to establish a finding of liability. If the district court did intend to reach a negligence decision, it did not set forth negligence law or make findings regarding that law. Further, it did not address the critical issue in negligence, the fault of the defendant. It addressed only the unreasonably dangerous nature of the product. Thus, any conclusion of negligence is unsupported.

Notwithstanding the existence of proximate cause, a manufacturer of a defective product can still be relieved of liability if some unforeseeable misuse or alteration occurred rising to the level of a superseding cause. **Prosser & Keeton** § 102, at 711. Marco and Martinac argue that such unforeseeable conduct occurred here.

They initially rely on a district court finding where the court purportedly stated that Saratoga Fishing's actions were a "precipitating cause" of the vessel's loss. Although the district court did make this finding, Marco and Martinac take it out of context. The court actually found that Saratoga Fishing's poor maintenance, misuse, and modifications to the hydraulic system "all contributed in some part to cause and bring about the catastrophic fire which ignited in the upper engine room . . . and was the precipitating cause of the vessel's loss . . . ." As this longer excerpt reveals, the court found that the fire was the precipitating cause of the loss. This is, of course, obvious. The court did not find that Saratoga Fishing's actions were a precipitating cause of the fire, rather it found that they were a contributing, or "substantial cause[ ]" of the fire.

[7] The district court did not find that Saratoga Fishing's misuse and alteration of the hydraulic system amounted to a superseding cause of the accident. The district court could have, but did not, find Saratoga Fishing's misuse to be unforeseeable.[9] *Cf. Kay v. Cessna Aircraft Co.*, 548 F.2d

[9]There was some controversy at trial over a water shield that was ostensibly installed over the turbocharger at the time the hydraulic system was installed on the SARATOGA. The district court was unable to determine whether this shield had been removed. It found however, that even if this shield had been in place, it would not have prevented the fire from igniting because it did not adequately cover the surfaces of the turbocharger and engine or isolate the hydraulic hoses from the surfaces. These findings are not clearly erroneous, and thus the presence or absence of the water shield does not affect Martinac and Marco's liability or affect whether Saratoga Fishing's actions constituted a superseding cause of the accident.

1370, 1372-73 (9th Cir. 1977) (plaintiff may recover if product is used in foreseeable, even if unintended use). The district court instead decided that hydraulic hose failure through either misuse, poor maintenance, or other conduct was foreseeable to Marco and Martinac, and that it would operate to reduce Saratoga Fishing's recovery but not to supersede Marco and Martinac's design defect as a proximate cause of the loss. This finding was not clearly erroneous.

[8] Marco and Martinac point to the alterations in the hydraulic system as examples that the system was modified substantially. The modifications, however, did not alter the design to the point where they superseded the design as a proximate cause of the fire.

D

Saratoga Fishing argues that the district court erred in reducing its award of damages by two-thirds based on the court's findings that it was also at fault for altering, misusing, failing to properly maintain, and ignoring the imminent failure of the hydraulic system. We agree with the district court.

[9] We have held that the concepts of "comparative fault (i.e., contributory negligence) . . . can be applied to the doctrine of strict products liability." *Pan-Alaska*, 565 F.2d at 1138. Under comparative fault principles, a party's blameworthy conduct that contributes to the proximate cause of the loss or injury will be compared to the defendant's liability and act to reduce the plaintiff's award of damages. *Id.* at 1139-40. As we stated: "It comes down to this: the defendant is strictly liable for the harm caused from his defective product, except that the award of damages shall be reduced in proportion to the plaintiff's contribution to his own loss or injury." *Id.* at 1139.

The district court found that Captain Vargas failed to properly maintain the hydraulic system. In an effort to increase the speed and power of the system, Vargas authorized enlarging the size of the seine, increasing the size of the power block, and increasing the velocity of the hydraulic flow and power to the machinery and equipment. This increased velocity raised the temperature of the hydraulic fluid and resulted in increased deterioration of the component parts of the hydraulic system, including the hydraulic hoses.

The district court also found that the engineers on board informed Captain Vargas that the hydraulic system was "overworked, wearing out and prone to an increasing number of failures." Vargas nonetheless continued to operate the system in excess of design pressures and temperatures and deferred remedial measures. Most significantly, the district court found that on January 16, the hydraulic hose that eventually failed was observed by the Chief Engineer and his assistant to be "leaking or weeping at the coupling."[10] Despite being informed of the problem with the hose, Captain Vargas continued to operate the hydraulic system. The district court found that this created an "unreasonable risk that the hose would fail," causing hydraulic fluid to come in contact with the surface of the engine.

[10] The poor maintenance of the system, the modifications to the system, and the use of the system known to have a

[10]Although Chief Engineer Nielson testified that he did not consider the defective hose to be dangerous, the district court found that the engineer must have been aware that it needed replacing and that the hydraulic system should not be operated. The district court also rejected Nielson's testimony that he was unaware of a risk of danger.

defective hose all contributed to the fire that caused the sinking of the vessel. The district court found that the conduct of those who manned the SARATOGA "border[ed] on irresponsible." The district judge is in the best position to weigh the evidence and apportion fault. *Alkmeon Naviera, S.A. v. M/V Marina L*, 633 F.2d 789, 796 (9th Cir. 1980). The district court's determination is not clearly erroneous and the apportionment of two-thirds liability to Saratoga Fishing will not be disturbed.

Saratoga Fishing next argues that Marco and Martinac failed to establish the standard of care of a prudent tuna boat operator. We reject this argument. Marco and Martinac presented substantial evidence concerning proper maintenance and care of a fishing vessel's hydraulic system. That is more than sufficient to establish a standard of care.

IV

We next address the subject of damages. The district court awarded Saratoga Fishing $452,326, which sum equals one-third of the combined value of the following items: the tuna catch, net, skiff, fuel, assorted equipment, crew losses, rescue costs, and cash. The district court declined to award damages for the value of replacement parts and the vessel's hull. Marco, Martinac, and Saratoga Fishing raise various objections to the award. We reject each of the arguments and agree with the district court's determinations.

[11] In *East River S.S. Corp v. Transamerica Delaval*, 476 U.S. 858 (1986), the Supreme Court recognized a significant limitation to its decision to adopt the law of strict products liability to admiralty. The Court drew a distinction between damage caused to the "product itself" and damage to a "person or other property." *Id.* at 870. When the product itself

is damaged, the "resulting loss is purely economic" and losses such as "repair costs, decreased value, and lost profits . . . essentially [involve] the failure of the purchaser to receive the benefit of its bargain—traditionally the core concern of contract law." *Id.* At least in the commercial context, the Court stated that damage to a product should be sought by plaintiffs through a contract or warranty claim. A cause of action for damages in a products liability claim in admiralty is available only for an injury to persons or "other property." *Id.*

We have not yet had the opportunity to further define the contours of "other property." The Fifth Circuit has stated that "the finished vessel delivered by the manufacturer to the purchaser is the product—the object of the contract . . . ." *Nicor Supply Ships Assoc. v. General Motors*, 876 F.2d 501, 505 (5th Cir. 1989) (quoting *Shipco 2295, Inc. v. Avondale Shipyards, Inc.*, 825 F.2d 925, 928-29 (5th Cir. 1987)). Because the equipment at issue in *Nicor* had been installed on the vessel after it had been delivered to the purchaser, the Fifth Circuit concluded that the equipment was not a product of the bargain between manufacturer and purchaser, and thus was "other property" for which damages could be recovered. *Id.*

[12] We agree with the Fifth Circuit's approach. Defining the product as the object of the contract between the manufacturer and purchaser comports with the language and policy of *East River*. A product liability plaintiff is not able to recover damages for economic losses resulting from the loss of the vessel, but can recover damages for items added to the vessel by its user. Because the *East River* court focused primarily on the role of warranty and contract law as the reason for limiting recovery of product liability damages, it is logical that when items are added to a vessel outside the scope of any warranty of contract between the initial purchaser and manufacturer, they are "other property."

Appendix D

A

[13] Marco and Martinac argue that most of the damages in the case, specifically the skiff, net, fuel, spare parts and miscellaneous equipment, were attributable to the product itself."[11] We disagree. Again quoting the Fifth Circuit, additions to a vessel should be considered other property "separate from the product that the manufacturer *originally* sold, if the distinction enunciated in *East River* between a 'product' and 'other property' is to have any meaning." *Nicor*, 876 F.2d at 506 (emphasis added). The key was whether the items were "part of the contract under which the vessel was sold." *Id.* Although all the aforementioned components were integral to the operation of the vessel, they were not part of the vessel that Martinac sold to McDruga in 1972. They were added later. Including these items as part of the "product" would undermine the "other property" exception contained in *East River*. Under that rationale, the product would envelop everything else useful in the operation of the vessel, which is not consistent with the balance struck by the Supreme Court. The items for which the district court awarded damages are inherently different from those component parts that were part of the vessel when it was delivered. The component parts were presumably accounted for in the contract to build the vessel. The district court correctly concluded that Saratoga Fishing was entitled to receive damages for the loss of those items including the net, skiff and miscellaneous equipment that were incorporated into the SARATOGA after the vessel was sold to McDruga. Furthermore, there is no clear error in the district court's findings regarding the amount of these damages.

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[11]The argument made by the defendants that some of the damages awarded were "economic loss" damages prohibited by *East River* is not correct. The district court awarded no damages based on "repair costs, decreased value, and lost profits." 476 U.S. at 870.

Appendix D

Marco and Martinac next argue that an award of damages for the tuna catch was unjustified. They contend that the lost catch was a nonrecoverable pure economic loss under various theories: first, because the lost catch was a work in progress; second, because the lost catch was equivalent to damaged cargo; and third because it was similar to failed or damaged crops. We disagree.

[14] The tuna catch that was destroyed was different than cargo because it was not being shipped from one site to another pursuant to a commercial agreement. It was new property on board the SARATOGA that belonged to the vessel's owner. The tuna was also not a work in progress as it had substantial value after being caught. The district court correctly reduced the value of the tuna by accounting for fuel costs and Panama Canal toll charges, and accurately computed the value of the tuna lying in the holds of the SARATOGA. Finally, the cases involving damaged crops are agricultural cases and are not helpful in the context of admiralty. We conclude that the tuna catch was not an economic loss, but was a loss of other property. The district court did not abuse its discretion in awarding damages for the tuna catch.

Marco and Martinac lastly contend that the district court erred in awarding Saratoga Fishing the value of Captain Vargas' lost currency because it was duplicative of sums awarded under the category of the lost crew property. The district court found that Vargas' testimony was "not effectively refuted" and was "credible." Marco and Martinac have shown insufficient evidence that the district court's findings were clearly erroneous. We will not disturb them.

B

Saratoga Fishing appeals the district court's refusal to award the value of replacement equipment installed in the vessel. It also argues that the district court erred in not permitting it to include the value of the vessel's hull in its damages sought from Marco.

[15] The district court concluded that replacement parts should not be recoverable as "other property" under *East River*. The court stated that permitting recovery would lead to the absurd result that the shipbuilder's liability would grow as the performance of the product's relationship to the shipbuilder decreased. We agree. Because a product may have any number of components replaced with spare parts in the ordinary course of events, viewing these parts as "other property" would lead to absurd results. Such results would be contrary to the policies of *East River*, where the Supreme Court expressed its intention to exclude damages to the product itself from tort law and leave the injured party to remedies in the law of contract and warranty. 476 U.S. at 871-72; *see Exxon Shipping Co. v. Pacific Resources, Inc.*, 835 F. Supp. 1195, 1200 (D. Haw. 1993) (prohibiting recovery of cost of replacement parts in admiralty products liability action).

Saratoga Fishing lastly seeks damages from Marco (not Martinac) for the loss of the vessel itself. This argument is based on two propositions: first, that the approach to damages in *East River* should not apply to fishermen; and second, that for a component manufacturer such as Marco, the only "product" is its hydraulic system and that the vessel is "other property." Neither argument has merit.

Saratoga Fishing relies on footnote 5 in *East River*, in which the Supreme Court observed that it had at times applied

a more protective approach in some admiralty contexts for fishermen, and that no fishermen were involved in that case. Even if that footnote reflected an exception to the rules set forth in *East River*, it is not applicable here. Saratoga Fishing is a company that owned an ocean-going tuna fishing vessel; there are no individual fishermen involved in this litigation. In any case, the only court that has considered the effect, if any, of the footnote, applied the *East River* damages rules without exception to a case involving plaintiffs who were fishermen. *McConnell v. Caterpillar Tractor Co.*, 646 F. Supp. 1520, 1525 (D.N.J. 1986).

Also without merit is Saratoga Fishing's argument that the vessel should be deemed "other property" relative to Marco because Marco designed a component part of the vessel. The Fifth Circuit has rejected a similar claim. In *Shipco 2295, Inc. v. Avondale Shipyards, Inc.*, 825 F.2d 925, 928 (5th Cir. 1987), *cert. denied*, 485 U.S. 1007 (1988), the Fifth Circuit rejected a damages claim against the designer of a component part, observing that there is "no rational reason to give the buyer greater rights to recover economic losses for a defect in the product because the component is designed, constructed or furnished by someone other than the final manufacturer." *Id.* at 929.

[16] This rationale is sound. Saratoga Fishing bargained for a fishing vessel. That is the product. *See Nicor*, 876 F.2d at 505 (finished vessel "delivered by the manufacturer to the purchaser" is the product). The hydraulic system is an integral part of the product. Seldom does one company design and build all component parts for an integrated product such as a fishing vessel. Permitting recovery from Marco for the vessel's hull would undermine the policy of *East River*—namely, that contract and warranty law should cover such losses, while tort law should be reserved for "other property."

C

Marco and Martinac argue that the district court erred in awarding prejudgment interest to Saratoga Fishing. They contend that Saratoga Fishing delayed filing a claim for almost two years after the vessel's loss and that Saratoga Fishing further delayed the litigation during a dispute over an attorney's conflict of interest.[12]

"In admiralty, prejudgment interest must be granted unless peculiar circumstances justify its denial." *McKay v. Rockwell Int'l Corp.*, 704 F.2d 444, 463 (9th Cir. 1983), *cert. denied*, 464 U.S. 1043 (1984). The determination of whether peculiar circumstances exist is left to the district court's sound discretion. *Id.* at 464.

Here, the district court concluded that this case was not "sufficiently peculiar or exceptional to justify departure from the general rule." Saratoga Fishing's claim was filed within the statute of limitations; thus, any delay was certainly not peculiar or unusual. The attorney conflict is also not an unusual occurrence. There is insufficient reason to disturb the district court's exercise of its sound discretion in awarding prejudgment interest.

Marco and Martinac also object to the district court's purported computation of postjudgment interest as inconsistent with the statutory mandate of 28 U.S.C. § 1961. Saratoga Fishing correctly points out, however, that the district court did not award postjudgment interest. It awarded additional

[12]Although Marco and Martinac initially objected to an award of prejudgment interest because of the high degree of Saratoga Fishing's comparative fault, they abandoned that ground on appeal.

prejudgment interest at the rate of $153.90 per day from the date of the damages findings and conclusions, June 1, 1993, until the date of final judgment, August 27, 1993. We find no error.

Finally, Saratoga Fishing is entitled to a further award of interest pursuant to 28 U.S.C. § 1961 from the date of entry of judgment until payment is made.

V

We are persuaded that the district court, having heard from all the experts and witnesses, did not err in deciding the issues of liability and damages. Marco and Martinac will pay their share because of their defectively designed hydraulic system, but Saratoga Fishing's award will be substantially reduced because of its failure to properly maintain and operate that system.

AFFIRMED

APPENDIX E — FINDINGS ON LIABILITY MADE BY THE DISTRICT COURT ON MAY 15, 1993

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF CALIFORNIA

Case No. 87-1691-F

SARATOGA FISHING COMPANY,

Plaintiff

vs.

J. M. MARTINAC & COMPANY, et al.,

Defendants.

FINDINGS AND CONCLUSIONS

Having reviewed the transcript of the findings and conclusions attached hereto, IT IS ORDERED the transcript be deemed my findings of fact and conclusions on liability.

DATED:

s/ James M. Fitzgerald
James M. Fitzgerald
United States District Judge

Appendix E

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF CALIFORNIA

Case No. 87-1691-F
Civil

SARATOGA FISHING COMPANY,

Plaintiff,

vs.

J. M. MARTINAC & COMPANY, et al.,

Defendants.

TRANSCRIPT OF FINDINGS AND CONCLUSIONS
Taken in San Diego, California
March 18, 1993

BEFORE THE HONORABLE JAMES M. FITZGERALD

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Appendix E

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF CALIFORNIA

Case No. 87-1691-F

San Diego, California

Thursday,
March 18, 1993

SARATOGA FISHING COMPANY,

Plaintiff,

vs.

J. M. MARTINAC & COMPANY, et al.,

Defendants.

TRANSCRIPT OF FINDINGS AND CONCLUSIONS
BEFORE THE HONORABLE JAMES M. FITZGERALD
UNITED STATES DISTRICT JUDGE

APPEARANCES:

For the Plaintiff: (Not present.)

For the Defendants: (Not present.)

Transcript Ordered by: HON. JAMES M. FITZGERALD

Appendix E

Court Recorder: Nancy Cablay
United States District Court
940 Front Street
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Transcriber: Mary Lou Lohr
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Proceedings recorded by electronic sound recording transcript produced by transcription service.

[1] SAN DIEGO, CALIFORNIA
TUESDAY, MARCH 18, 1993

—oOo—

(Call to order of the Court.)

THE COURT: We'll begin with the findings and conclusions on the liability issues relating to Saratoga Fisheries versus Martinac Shipyards and Marco.

The findings and conclusions will be taken from notes, memoranda and excerpts of authority which I have reviewed and, after the findings and conclusions have been placed of record, the original transcript of the findings and conclusions will be filed with the clerk of the court for record.

I'd like a copy of the findings and conclusions to go to Judge Thompson who has managed the case up until it was assigned to

me for trial, and I would like a copy so that I may address any post-trial motions.

Parties may, of course, order copies of the transcript or may copy the transcript provided it has once been filed with the clerk of the court.

I'll begin now with the findings which will be numbered, followed in general by the conclusions. Each finding identified by number will be separately set out and will be separated by double spacing. Quotes, and I shall refer to quotes from time to time, shall be single-spaced in the findings or conclusions.

[2] FINDINGS

(1) The *Saratoga*, a tuna fishing vessel, was constructed at the Martinac Shipyard, Seattle, Washington. The vessel was built in 1971 on order for and old-time fisherman, Joseph McDruga, and it was to be the third tuna boat built for him by Martinac. At least part of the machinery installed aboard the *Saratoga* was according to his choice.

The hydraulic drive powering the power block and winches and other machinery on the *Saratoga* was a D333 Caterpillar engine connected to a MARCO hydraulic system.

The D333 Cat was considered at the time to be a fine diesel engine when operated within its capabilities.

(2) Commercial tuna fishing in earlier times had been done with poles, fishing lines and hooks fished from the deck of the boat by a crew.

As the tuna fishery evolved, nets or seines were put aboard boats which enabled the taking of large quantities of fish. Power blocks and winches necessary to purse the seine or net or to brail the fish and to take the seine aboard after completion of a set were installed in tuna boats.

(3) MARCO Seattle was in the business of [3] providing marine equipment and marine systems to commercial fishing fleets and MARCO Seattle had designed a hydraulic system to operate the machinery and equipment used in tuna fishing operations.

(4) Martinac Shipyards often installed MARCO products, machinery and MARCO hydraulic systems in construction of tuna vessels. Martinac Hull 188 became the *Saratoga* owned by Joseph McDruga.

(5) After consultation with Joseph McDruga or his representatives, Martinac contracted with MARCO Seattle for a MARCO hydraulic system including pumps, pump drives, control valves, winches, pressure gauges and a Caterpillar D333 diesel engine for the *Saratoga*.

(6) The Caterpillar engine had been manufactured by Caterpillar Tractor, sold to Northern Commercial Marine in Seattle and then to MARCO Seattle. The evidence at trial persuaded me that Caterpillar had taken no part in the design of the hydraulic system installed on the *Saratoga* and that the engine as sold was not defective either in manufacture or design.

I concluded that Caterpillar should not be required to contribute in any way to any loss claimed in [4] this trial.

(7) The installation of the MARCO hydraulic system on the *Saratoga* was done at the Martinac Shipyard according to the drawings provided by MARCO. After the hydraulic system was installed, MARCO had agreed to inspect the installation of the system on the *Saratoga*, to determine whether the hydraulic system had been properly installed and to make certain the equipment operated in accordance with the hydraulic system design.

MARCO charged and was paid a fee for performing these contractual obligations. MARCO also prepared an instruction manual containing hydraulic circuit diagrams, detailed parts lists and breakdowns.

(8) The *Saratoga* was launched in January 1972 and underwent sea trials in Puget Sound. Joseph McDruga and his representatives including Manuel Vargas attended and, although MARCO representatives were aboard during the sea trials, the MARCO people were primarily observers.

Manuel Vargas as McDruga's representative requested Martinac Shipyards to reposition some cleats on the *Saratoga* and to change the placement of the hoist for the speedboats. The McDruga representatives were not marine designers, but worked aboard tuna vessels as [5] engineers or crew.

After the sea trials were completed, the McDruga captain and crew boarded the *Saratoga* in Puget Sound and brought her to San Diego where net trials would customarily have taken place.

MARCO representatives usually attended the net trials for the purpose of monitoring the hydraulic system, equipment and machinery, or to make any modifications or repairs.

(9) However, in this instance, net trials were not undertaken in San Diego at that time. A quota system had been adopted in the tuna fishery, and it was necessary to ready the *Saratoga* for fishing operations in order for the *Saratoga* to obtain a share of the quota.

Manuel Vargas went aboard the *Saratoga* in San Diego as captain and took the vessel to Panama where a seine or net and other fishing equipment were put aboard the *Saratoga* and, when properly equipped, she put to sea ready to fish in order to qualify for a share of the authorized quota.

(10) Later, when the *Saratoga* returned from its initial fishing voyage to San Diego, National Pump and Injector performed warranty work on the MARCO hydraulic [6] system by making adjustments or corrections to the system.

The warranty work done by NPI was on account from MARCO Seattle and had been authorized to be done by NPI at MARCO's expense.

Often during net trials, MARCO personnel attended and performed warranty work including adjustments to the hydraulic system.

(11) In March of 1974, the *Saratoga* was purchased from Joseph McDruga's fishing company by Vargas Fishery, a company of which Manuel Vargas was then principal owner and officer. At the time the *Saratoga* was acquired by Vargas Fishery, the vessel carried a full stock of equipment, spare parts and tools.

(12) Vargas knew the *Saratoga* well and no representation as to the fitness or condition of the vessel was offered or

requested. Vargas at the time of sale was fully satisfied in the condition of the vessel including its hydraulic drive system.

The *Saratoga* when purchased by Vargas Fishery was equipped for tuna fishing with five speedboats, outboard motors, a purse skiff, a seine or net, two sideband radios, radar and other electronic equipment, a VHF direction finder and a 42-inch power block.

[7] (13) Manuel Vargas continued as captain to fish the *Saratoga* until 1979. In that year Vargas became captain of another vessel and his son-in-law, Arthur Ferreria, became captain of the *Saratoga*.

In late 1983, the *Saratoga* was tied up at a dock for four or five months. In January 1984 Vargas again became captain of the *Saratoga*. The vessel was at that time in poor condition, and Vargas spent considerable amounts of money to improve the vessel's condition and machinery to bring her, according to his terms, back up to what she once was.

From January 1984 until the loss of the *Saratoga* in January 1986, Vargas estimated that he spent $175,000 on the vessel, her machinery and equipment.

(14) A number of modifications were made to the machinery and equipment originally installed on the vessel during the period from January 1984 until the time she was lost. The net size was increased; a single and double winch were mounted on the boom; a new boom with larger hydraulic hoses replaced the boom which had been originally placed board the vessel. A larger power block of 48 inches was installed. Larger cartridges were put into the Vickers pumps driven by the

hydraulic drive, and a 100-horsepower electric drive and pump were instal!ed to increase power [8] and flow in the hydraulic system in addition to the original 190-horsepower D333 Caterpillar engine.

(15) On December 23, 1985, the *Saratoga* came to Panama from a fishing voyage. The turbocharger on the in engine had failed, and repair of the turbo was necessary. Captain Vargas left the vessel while it was undergoing repair in Panama to spend the holidays with his family.

(16) The *Saratoga* departed Panama on January 8, 1986 to return to the fishing grounds. During fishing operations some 200 miles off the Gallapagos Islands, at approximately 6:00 p.m., January 16, 1986, a fire ignited in the upper engine room when a hose ruptured or released from the coupling attached to the pump.

(17) Within minutes the fire expanded into the lower engine room. Efforts were made by the chief engineers and others of the crew to suppress the fire, but Captain Vargas concluded after 10 to 20 minutes that efforts to put the file out were futile, and he ordered the *Saratoga* abandoned.

The crew quickly boarded into the first skiff and within a few hours were rescued by the *Chiriqui II*. [9] The next morning, January 17, 1986, shortly after 8:00 a.m., the *Saratoga* sank.

(18) The claimant in this maritime case is Saratoga Fisheries. The respondents are MARCO Seattle and Martinac Shipbuilding. The claim is in tort for loss of property. Other claims have been disposed of.

(19) According to David Saveker, a well qualified naval architect, the MARCO hydraulic drive system, in his expert opinion, incorporated an unsafe design and, according to his words, was an accident waiting to happen.

According to Saveker, the hoses and fittings in hydraulic systems are prone to failure, and it is not enough to rely upon maintenance of the system or fire suppression to accomplish a safe design.

Saveker found that MARCO had failed to do a hazard analysis or to examine failure modes at the time the MARCO hydraulic system was designed.

(20) Larry Grief, a qualified marine architect, is president of a private company which designs, among other things, hydraulic systems, electrical systems and the like for commercial vessels. His company has designed [10] hydraulic systems for tuna vessels.

Grief had examined the plans and specifications of the *Saratoga* including the hydraulic system, the CO_2 system and the piping and water cooling systems installed aboard the *Saratoga* at the Martinac Shipyard. He had reviewed numerous depositions and statements of former crew members on the *Saratoga*.

(21) On the basis of his examination and investigation, Grief formed the opinion that, at the time the hydraulic system was installed on board the *Saratoga*, the system as designed met well established marine practice and all requirements for commercial or naval vessels.

Indeed, Grief testified that the hydraulic system as designed and installed aboard the *Saratoga* was similar to hydraulic systems on virtually every vessel he had been aboard.

(22) There's no doubt Grief had been aboard and is extremely knowledgeable about the construction of commercial vessels and the equipment or machinery installed on such vessels. He served in the Coast Guard in a number of positions. He was chief engineer on a Coast Guard cutter off Vietnam during the Vietnam War, and he has served as a Coast Guard inspector of commercial vessels.

[11] Grief has attended Coast Guard training programs and shipboard damage control, firefighting and fire suppression. Due to his varied experience as a Coast Guard officer and his participation in the construction and inspection of commercial vessels, Grief also had a good deal of knowledge about Coast Guard regulations and the application of those regulations to commercial vessels including tuna vessels.

He's also familiar with industry trade rules such as those published by the American Bureau of Shipping.

(23) After examining the plans, specification and drawings of the MARCO hydraulic system, Grief found the flow rates and pressures as designed for the system well thought out. Sufficient information was found in the documents to permit analysis of the capabilities and reliability of the hydraulic system.

(24) At the time the *Saratoga* was constructed in the Martinac Shipyard, it was recognized and accepted within the commercial shipbuilding industry that the isolation of all flammable or combustible liquids in the engine room was not possible.

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Diesel oil, a flammable liquid, must be brought to the engine. Hoses which carry fluids are sometimes [12] attached directly to the engine or in close proximity to the engine. Metal piping carrying fluids is subject to failure in much the same way as are hoses. Metal piping may fail at connections or in fittings.

The solution adopted by the commercial shipbuilding industry to reduce risks posed by flammable or combustible liquids in proximity to engines was to design into marine systems or components a safety factor of 4 to 1.

(25) MARCO, in keeping with the industry practice, specified components in the MARCO hydraulic system in full compliance with the prevailing standards at the time, but MARCO also increased the safety factor on hydraulic hoses by specifying the hoses to meet 3,000 psi pressures, thus increasing the safety factor over and above that accepted by the industry.

The velocity of the flow designed within the MARCO hydraulic system was in keeping with industry standards aimed at maintaining temperatures of hydraulic fluid at 135 degrees or below.

(26) At the time the *Saratoga* was built in the Martinac Shipyard, the hydraulic design provided by MARCO and installed by Martinac Shipyard met well established [13] marine practice.

(27) Grief's testimony on these issues was credible and reliable. He has a great deal of knowledge and experience by reason of his training and background in the application of the Coast Guard regulations of industry practice and rules having to do with the design and construction of commercial vessels.

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(28) David Saveker is a fully qualified naval architect, but his background is primarily in the construction and equipping of naval vessels. However, as Grief testified, there is considerable difference between standards which apply to naval vessels from those applicable to commercial vessels.

Obviously, the mission of naval vessels differs from the purpose of commercial shipping.

(29) Grief's opinion concerning the regulations and standards applicable to the *Saratoga* at the time the vessel was constructed are entitled to full credit. The hydraulic system designed by MARCO and installed by Martinac Shipyard on the *Saratoga* met all regulatory requirements and all trade and standards accepted and followed in the shipbuilding industry at the time the [14] *Saratoga* was constructed.

(30) Since risks and hazards, according to Grief, are met in the commercial shipbuilding industry by incorporating standards providing a safety factor of 4 to 1; that is, hydraulic hoses and other components must be specified to withstand pressures and perhaps temperatures in excess of four times normal operating conditions.

(31) Standards in the commercial shipbuilding industry did not at the time the *Saratoga* was constructed require a hazard analysis for consideration of potential failure modes.

(32) The evidence in fact does establish that MARCO designers were aware that the rupture or failure of a hydraulic hose or failure of a coupling on a hydraulic system operating at 2,000 psi in close proximity to an engine operating with surface temperatures in excess of the flash point of hydraulic fluid created a serious risk of fire.

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(33) MARCO designed the hydraulic system with reference to existing standards and manufacturer's ratings on hoses and fittings to minimize the possibility of [15] failure and to reduce the possibility of accidental escape of hydraulic fluid from the system.

MARCO did not recommend placement of a metal barrier or other means of isolating the hydraulic hoses coming off the pumps from the D333 Caterpillar engine or the turbocharger.

(34) According to the opinion of naval architect, David Saveker, the designer of the MARCO hydraulic system failed to do a hazard analysis or to examine potential failure modes.

It was known according to Saveker that hydraulic hoses and couplings will fail, and it's not enough to rely upon maintenance of the hydraulic system or control of fire by means of fire suppression. Rather, in Saveker's opinion, it was necessary for the designer of a hydraulic system to undertake a hazard analysis and cause the hazard to be removed from the system or otherwise to provide adequate warnings. Failure to do so at the time the MARCO hydraulic system was designed caused the system to be unreasonably dangerous and was a direct cause of the fire and loss of the *Saratoga*.

(35) Based on his investigation and study, Grief found the CO_2 system as designed and installed on the [16] *Saratoga* to be in compliance with well established practice in commercial vessels and fully complied with Coast Guard regulations.

The CO_2 system installed in the *Saratoga* was state of the art in 1972. Periodic surveys of the vessel including a survey done following work in 1985 at Ensenada Shipyard revealed the CO_2 system was inspected and found in good operating condition.

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(36) However, based upon his investigation including examination of deposition testimony as well as the plans, specifications and drawings of the *Saratoga*, Grief formed an opinion that at the time of the fire aboard the *Saratoga*, the CO_2 system was not activated. The siren failed to sound although it was connected into the system, and the blowers installed to ventilate and exhaust the engine rooms failed to shut down.

CO_2 did not release into the engine room since Grief determined that the *Saratoga*'s generating system continued to function for approximately an hour. If CO_2 had released into the engine room, the power drive to the generator would have stopped within minutes for want of oxygen.

(37) The design of the CO_2 system provided an [17] automatic closure of a door between the shaft alley and the main engine room. Again, based upon his investigation into the cause of the loss of the *Saratoga*, Grief found no indication that the door closed, and he found that, had the door closed, the shaft alley would not have flooded.

According to Coast Guard tests on CO_2 systems, the CO_2 system would have contained 2,400 pounds of CO_2 and 85 percent of the total CO_2 in the system would have released into the engine room, and diesel-driven engines would stop within two minutes for want of oxygen.

(38) I accept Grief's opinion that the CO_2 system aboard the *Saratoga* was state of the art when installed. I agree as well with his opinions that the CO_2 system was not activated or did not function at the fire ignited in the upper engine room of the *Saratoga* on January 16th for the reasons given by Grief.

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(39) David Saveker expressed his opinion that Martinac's use of plastic pipe below the water line of the *Saratoga* was a defective design and unreasonably dangerous. However, he had no knowledge of industry standards or regulatory codes regarding the use of plastic pipe in commercial tuna boats in 1972. In his opinion, the fire had expanded into the lower engine room and melted the [18] plastic pipe within three to five minutes after the fire ignited. The damage to the plastic pipe caused the *Saratoga* to flood.

(40) Antoine Jasick, an expert fire investigator, also expressed his opinion that the plastic pipe was involved by fire within four to six minutes and at that time the vessel began flooding through the plastic pipe.

(41) Larry Grief reviewed Saveker's opinions relating to the cause of the flooding of the *Saratoga* and the ultimate loss of the vessel. He found that Saveker's opinion on the cause of the flooding was not based on adequate information or data to support Saveker's conclusions.

According to Grief, without detailed examination of the construction plans of the vessel and knowledge of access or openings into the hull, estimates to the cause or rate of flooding cannot be made with any degree of reliability.

(42) At the time the *Saratoga* was built, the construction plans for sea water service piping in the lower engine room was steel, and the PVC pipe or plastic [19] piping was installed into the brine lines outside the engine room.

According to Chief Engineer Ogilvie, the sea water service lines were steel from the sea chest to the pumps and beyond the pumps were plastic pipe.

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When Grief made his investigation, he concluded that plastic pipe had replaced steel piping in the engine room of the *Saratoga*.

(43) PVC piping is universally accepted and is considered good practice to install in commercial vessels including tuna boats with the exception of critical services such as to main propulsion engines and to firefighting systems.

A brine system installed board a tuna boat is not considered a critical service. Not only do the Coast Guard regulations permit the use of plastic pipe in commercial vessels, but the American Bureau of Shipping Rules permit the use of plastic pipes in non-vital systems.

Metal piping is subject to corrosion, and plastic pipe is easier for a crew to repair while a vessel is at sea. It is not uncommon in a warm, salt-water environment to find it necessary to replace metal piping after 10 years.

[20] (44) Grief examined documents containing details of the *Saratoga*'s construction. According to the plans of the *Saratoga*, plastic pipe was specified for use in the brine system. Piping in the main engine room, according to the plans, is steel until the piping enters the shaft alley.

Grief found the use of plastic pipe in the brine system an excellent choice and in full accord with regulations and rules at the time the pipe was installed.

(45) Grief also found the CO_2 system as designed for the *Saratoga* to be in compliance with well established practice in commercial vessels and met Coast Guard regulations accepted

within the industry. The *Saratoga* CO_2 system was state of the art in 1972.

(46) The design of the hydraulic system installed aboard the *Saratoga* met well established marine practice and met design requirements of commercial and naval vessels. According to Grief, the hydraulic system design installed aboard the *Saratoga* was similar to hydraulic systems present in virtually every vessel he'd been aboard.

(47) I find that the opinions of Saveker and [21] Jasick as to how the flooding occurred on the *Saratoga* are not supported by underlying information or data, and I reject their opinions.

The cause of the flooding on the *Saratoga* cannot be determined within a reasonable degree of probability, but I find the use of plastic pipe in a brine system in *Saratoga* as installed in the shipyard was not a design defect which contributed, caused or brought about the flooding and the loss of the *Saratoga*.

(48) When the *Saratoga* was in the shipyard in Ensenada in 1985, work was done on the vessels hull including sandblasting. After the vessel returned to the fishing grounds, Captain Vargas noted that the pump cartridges, quote, "wore out like crazy", end of quote.

He requested the chief engineer to look into the problem and, upon inspection by the engineer, sand was found in the filter fluid reservoir or tank.

(49) But sand or grit if very difficult to remove from hydraulic systems. Sand or grit destroys or damages pumps, valves and other machinery. Sand will collect in small orifices and cause valves to stick and not open.

The efforts of the engineers aboard the *Saratoga* [22] to clean the hydraulic system of sand or grit was not entirely successful. Attention to the problem had followed Captain Vargas' observations that the cartridges in the Vickers pumps were wearing out an abnormal rate.

After the hydraulic system was cleaned, the pump cartridges in the Vickers pump continued to wear out within a short time, far less time than normal on tuna vessels.

(50) Vesley Ogilvie boarded the *Saratoga* as chief engineer at San Diego early in May of 1984. At that time the vessel was in poor condition and was undergoing some repairs at dockside. The Caterpillar D333 engine driving the hydraulic system was overhauled. Ogilvie replaced hydraulic hoses and cleaned the system up.

On the first trip out after dock repairs, considerable trouble was experienced in the hydraulic system including loss of power. Valves were leaking and hoses breaking on the deck.

Ogilvie's opinion on the cause of hydraulic system problems was that the system was worn out.

(51) During fishing operations, the hydraulic system was not pursing the seine as fast as Captain Vargas wished. Captain Vargas wanted more power from the equipment during operations and the auxiliary 100- [23] horsepower electric drive and pump were installed to provide more power to the power block. But adding the electric drive pump did not solve the problem. The power block was not rotating as fast as Captain Vargas wanted, so Ogilvie changed to larger cartridges in the Vickers pumps in order to increase power on the system.

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Two of the pumps were double pumps and Ogilvie installed cartridges providing more flow of the hydraulic fluid on each side of these two main pumps. In addition, a single-cartridge pump is driven off the hydraulic drive, and Ogilvie also installed a larger cartridge in the single pump. Although pressure increased in the hydraulic system, there was little improvement in the pursing of the seine. The problems persisted.

(52) In an effort to increase power as Captain Vargas wished, Ogilvie increased the pressure on the system to 2,400 psi on the main purse winch and the power block. Ogilvie advised Captain Vargas that, in Ogilvie's opinion, the hydraulic lines installed aboard the *Saratoga* were too small and a larger, stronger engine was needed for the hydraulic drive. Captain Vargas priced the costs and expenses for a more powerful engine.

(53) Lewis Jorge came aboard the *Saratoga* as [24] assistant engineer in July of 1985. On his first trip out aboard the *Saratoga*, Jorge observed the D333 Cat engine overheat and pump cartridges were wearing out.

Chief Engineer Ogilvie and Assistant Engineer Jorge continued to change cartridges in order to obtain a maximum amount of hydraulic flow in the system. Although the performance of the pumps and the hydraulic system had been enhanced by inserting larger cartridges, the hydraulic system failed to perform well. On almost every set, problems were encountered. In Jorge's opinion, the system was overloaded.

(54) Sometimes while pursing the seine, the water temperature gauge on the D333 Cat went into the red and the engine occasionally shut down. Efforts were attempted to cool the engine by injecting water into the cooling system with a fire hose.

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The alarm panel installed on the engine was activated by high water temperatures in the engine. Because of the annoyance caused by the alarm sounding frequently, the alarm system was switched off.

(55) When the *Saratoga* came into Ponce, Puerto Rico in October of 1985, Ogilvie left the vessel and Chief Engineer Mark Nielsen replaced Ogilvie. The *Saratoga* was [25] unloaded tuna at the time Nielsen came aboard.

(56) After leaving Puerto Rico, the *Saratoga* was to proceed to Panama for work on the hydraulic system. Several of the winches were leaking hydraulic fluid. Several hydraulic hoses needed replacement. The D333 Cat engine was overheating, but the operating plan of Captain Vargas was to live with that problem until the next shipyard overhaul. Money was short since considerable had been spent to make other repairs to the vessel.

(57) Captain Vargas discussed with Chief Engineer Nielsen the heating problems, the inadequate engine size, but said those matters would be taken care of at the next shipyard layup. Captain Vargas planned to change the engine for a larger size and install a more adequate heat exchanger.

(58) Nielsen brought to Captain Vargas' attention the heat temperatures of the hydraulic fluid in the hydraulic system. Readings were taken indicating hydraulic fluid temperatures of 210 degrees Fahrenheit and 215 degrees Fahrenheit.

Nielsen also called Captain Vargas' attention to the manuals which indicated normal operating temperatures [26] of 125 degrees Fahrenheit to 140 degrees Fahrenheit.

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(59) When the *Saratoga* arrived in Panama, MARCO Panama was engaged to do the work on the hydraulic system. The system was pressure-checked to determine the source of power loss. Several pump cartridges were found defective and were replaced. Work was also done on deck hydraulic machinery, and several seals in the hydraulic system were replaced. The repairs took approximately one week.

(60) The seals in the hydraulic system were designed to operate at normal procedures in the system. Excessive heat causes accelerated deterioration of seals and some other components such as hydraulic hoses. Indeed, Chief Engineer Nielsen testified that excessive heat in the hydraulic system leads to a multitude of problems. He observed that the Vickers pump manuals teach that Vickers pumps will break down very rapidly at high heat. Excessive heat in the hydraulic system reduces the viscosity of the hydraulic fluid and under pressure will cause metal wear in pumps. Loss of lubrication capacity can increase violation.

Hydraulic hoses are installed in hydraulic systems to isolate the vibration of moving engines or machinery from other parts of the hydraulic system that are [27] static or mounted on the vessel.

(61) Nielsen noted that the drawings and blueprints supplied by the shipyard for the original hydraulic system call for smaller-capacity cartridges in the Vickers pumps, but the increased capacity provided by the larger cartridges provided, in Nielsen's opinion, an increased flow of 25 to 30 percent.

(62) Not only was the hydraulic fluid temperature exceeding normal operating limits, but the main drive engine,

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the D333 Cat was overheating. The water temperature alarm had been turned off on the engine to eliminate the annoyance caused by the alarm which often sounded. At times, while fishing operations were ongoing, the main hydraulic drive, the D333 Cat, would shut down because of excessive water temperature.

(63) Depending on the engine horsepower, the hydraulic system can operate hydraulic pumps, machinery and equipment by driving a given amount of hydraulic fluid at a given pressure. Changing the pump cartridges to larger-sized cartridges will provide more power since the velocity of the hydraulic fluid will be increased. This in turn will lead to greater friction and more heat.

[28] (64) After the *Saratoga* left Panama for the fishing grounds, the pump cartridges installed by MARCO Panama wore out and needed to be replaced. In Nielsen's experience, the normal life of pump cartridges would be expected to be several years, and failure of the pump cartridges within such a short time would be abnormal.

(65) In Griefs opinion, the hydraulic system aboard the *Saratoga* was no longer operating by reason of the modifications put into the system as the system had originally been designed. The 100-horsepower electric drive and pump amounted to a major change in the hydraulic system causing the hydraulic fluid to pass through the system at higher velocity. Larger equipment such as the 48-inch power block requiring more power to operate had been installed without modification of the hydraulic hoses, piping and relief valves.

Temperatures of the hydraulic fluid reached as high as 215 degrees Fahrenheit, far higher than the maximum of 160 degrees

Fahrenheit with an operating range of 100 degrees Fahrenheit to 140 degrees Fahrenheit as designed into the system.

Temperature of 215 degrees Fahrenheit as noted by the engineers aboard the *Saratoga* would not have been reached had the hydraulic system been operating in [29] accordance with the original design.

The high temperatures of the hydraulic fluid necessarily would impact upon the pumps, relief valves and other machinery operating with close tolerances and working parts.

(66) As temperatures of hydraulic fluid increased, the viscosity of the fluid decreases causing greater wear. High temperatures of the hydraulic fluid affects not only machinery or equipment but hydraulic hoses, fittings, seals and the like.

The primary effect of heat on all of these components is to increase the rate of deterioration.

(67) The *Saratoga* was again forced to return to Panama on the 23rd of December because the turbocharger on the main engine failed. After some two weeks in Panama undergoing repairs, the *Saratoga* departed Panama on January 8th to fish approximately 200 miles of the Gallapagos Islands.

(68) On January 16th, Chief Engineer Nielsen observed the one and one-quarter-inch hydraulic hose seeping hydraulic fluid between the hose and the coupling attached to the pump. Nielsen would have made up a new [30] hose but lacked a necessary tool. He took the matter up with Captain Vargas, and the *Chiriqui II* was contacted by radio.

It was arranged that the needed replacement hydraulic hose would be made up on the *Chiriqui II*, and a meeting between the two boats was scheduled for later that day.

A few days earlier, a smaller, three-quarter-inch hydraulic hose had been replaced by Assistant Engineer Jorge. The tools necessary to make up the three-quarter-inch hydraulic hose were aboard the *Saratoga*.

(69) Assistant Engineer Jorge had also observed that the hydraulic hose on board on the port side pump of the *Saratoga* hydraulic system was leaking hydraulic fluid. He recalled that the engineers searched for a proper size crimping tool, but the necessary tool could not be found.

(70) In the afternoon, tuna were observed, and Captain Vargas ordered a set to be made. Ordinarily, Arthur Ferreria would operate the controls pursing the net. However, a radio schedule with the tuna fleet or as termed the code boats was to begin at 6:00 p.m. At that time, Captain Vargas took over the controls at the console.

Ordinarily, if a substantial catch is made, the [31] seine is pursed and the tuna are brailed from the net bag to the vessel. The catch was not heavy, and Captain Vargas brought the net and the fish aboard. Before the fish were lowered to the deck, Captain Vargas complained to Chief Engineer Nielsen that he was having trouble with the single winch which had completely lost power.

When Vargas moved the control on the double winch, the single winch momentarily functioned, but within approximately a half a minute, the single winch malfunctioned again.

(71) While these events were occurring, Assistant

Engineer Jorge was on his way to adjust the pumps in order to put brine into the tank receiving the catch. As he passed through the upper engine room, he saw the one and one-quarter-inch hydraulic hose nearest the port side pulsating. Jorge had never before observed the hydraulic hose pulsing. This attracted his attention and, as he watched, the hose pulled out of the coupling and almost immediately hydraulic fluid sprayed to the overhead and onto the turbocharger and ignited.

(72) Jorge attempted to turn the engine shutoff lever but was unable to stop the engine before he was driven away by flames. He attempted to suppress the fire [32] with a CO_2 handle bottle, but the flames continued to expand in the engine room, and he left the engine room to make his way forward and out a hatch onto the deck.

(73) Chief Engineer Nielsen had by this time activated a fire hose and was attempting to extinguish the fire, standing on a ladder which descended to the wet deck. Smoke was pouring out of the access door to the upper engine room, so Chief Nielsen went to get an air mask carried on board and, after putting the mask on, attempted to descend to the wet deck. However, the water failed in the fire hose.

(74) Assistant Engineer George recalls that he went forward to activate the CO_2 system. He found it necessary to break the glass face over the pull cable, but was able to pull the handle attached to the cable which should have immediately released CO_2 into the engine room.

When he pulled the handle, the cable moved, but he observed no effect from the CO_2 system.

(75) Fire Investigator Jasick was of the opinion that the

pressure on the hydraulic system caused the hydraulic fluid to atomize causing the vapor to ignite on contact with the turbocharger.

[33] There is considerable doubt whether the pressure after release of the hydraulic hose from the coupling may have been sufficient to atomize the hydraulic fluid.

(76) The two experts, Saveker and Grief, disagree whether the pressure in the system was sufficient to project the fluid up to the overhead, but I find the hydraulic fluid on release of the hydraulic hose sprayed up from the coupling, fell back on the hot surfaces of the turbo and immediately ignited.

The fire investigator estimated that the entire upper engine room was enveloped with fire within one minute. Again, I believe that this opinion is subject to considerable doubt in view of Assistant Engineer Jorge's efforts to shut down the engine and to obtain the CO_2 bottle which he had discharged or emptied in the engine room before he fled.

(77) Investigator Jasick came to the opinion that hydraulic fluid escaped into the lower engine room and ignited within 30 seconds to one minute. He also reached opinions that the closing of the access door to the upper engine room, the shutting down of the blowers and the activation of the CO_2 suppression system would not have made any difference; the fire could not have been [34] suppressed.

(78) When Captain Vargas became convinced that the flames were spreading on the vessel and the fire could not be controlled, he ordered the crew to abandon the *Saratoga*.

The crew took the first skiff alongside the *Saratoga*, leaving

behind their personal effects. No member of the crew sustained injury, but Assistant Engineer Jorge suffered some minor burns. Arthur Ferreria retrieved the *Saratoga*'s papers. Captain Vargas carried a radio aboard the seine's skiff but was unable to open the ship's safe and left $16,000 on board.

(79) Approximately three hours later, the *Chiriqui II* appeared and rescued the crew. The following morning, January 17th 1986, shortly after 8:00 a.m., the *Saratoga* sank.

Obviously, the immediate cause of the *Saratoga*'s sinking was the flooding that occurred in consequence of the fire. Because of the uncertainty in the evidence, I am unable to say precisely how the flooding occurred except that I am able to find that it was caused by the fire.

The *Chiriqui II* sailed for Costa Rica to put the [35] crew of the *Saratoga* ashore. The master of the *Chiriqui II* was unwilling to tow the *Saratoga*'s purse skiff, which was then scuttled.

(80) Saratoga Fishing contends that National Pump and Injector and MARCO Panama were agents of MARCO Seattle. Hence, any modifications in the hydraulic system which was designed and furnished by MARCO Seattle and installed by Martinac Shipbuilding that were recommended by National Pump and Injector or MARCO Panama are the responsibility of MARCO Seattle.

(81) Authority to act as an agent can be created by words or other conduct on the part of the principal causing the agent to believe that the principal intends him to act for the principal's account. See Restatement Second of Agency, § 26.

Saratoga Fishing, however, is not relying upon the doctrine

of actual authority to establish the responsibility of MARCO Seattle for modifications of the hydraulic system aboard the *Saratoga*. Rather, Saratoga Fishing contends that MARCO Seattle may be held responsible for the modifications to the hydraulic system of the *Saratoga* under the doctrine of apparent authority.

Apparent authority is created as to a third [36] party by words or conduct of the principal which, reasonably interpreted, caused the third party to believe that the principal consents to have the act done on his behalf by the person purporting to act for him. See Restatement of Agency Second, § 27.

(82) In order to recover against MARCO Seattle on this theory, Saratoga Fishing must establish:

(1) The principal was responsible for the appearance of authority in the agent to conduct the transaction.

(2) The third party reasonably relied upon the representations of the agent.

However, the existence of apparent authority must be due to the words or conduct of the principal and cannot be established by the unauthorized acts, representations or conduct of the agent.

(83) I find that Guy Bruni of NP&I was not authorized by MARCO Seattle to act as its agent, and the only instance that NP&I was authorized to act as MARCO's representative was in performing warranty work after the *Saratoga* returned to San Diego from making its first voyage out.

[37] (84) The insertion of the larger cartridges in the Vickers pumps was done initially by Chief Engineer Ogilvie in

order to respond to Captain Vargas demand for more power to the power blocks, winches and other machinery.

CONCLUSIONS

(85) I conclude that neither NP&I nor MARCO Panama had either expressed authority, nor did MARCO Seattle, by words or conduct, represent or suggest to Saratoga Fisheries that NP&I or MARCO Panama were authorized to act for or represent MARCO Seattle in any way during the period of 1984 until the time the *Saratoga* was lost in January of 1986.

(86) Saratoga Fisheries advances claims of liability on theories of negligence, strict products liability and failure to warn. On the evidence presented at trial, the strict product liability and negligence claims come down to the same two questions, albeit phrased in different terminology.

(87) Joseph Martinac, president of Martinac Shipyards, testified that he knew at the time the *Saratoga* [38] was built of the danger of a fire from hydraulic hose failure. The design choice to counter this risk was to build in a safety margin in the components of the hydraulic system from four to six times the maximum pressures.

(88) This concession reduces issues of negligence and unreasonably dangerous product to the single question of whether the choice selected was a reasonable design. Quote:

> "The strict liability standard is no different from that of negligence . . . except that the seller is presumed to have knowledge of the actual condition of the product when it leaves his hands."

See Phillips, *The Standard for Determining Defectiveness in Products Liability*, 46 U.Cin.L.Rev. 101 at 103 (1977), citing to Deans Wade and Keeton.

(89) The modifications and claimed misuse of the hydraulic system by the claimant, Saratoga Fisheries, whether phrased as a foreseeable misuse question in strict products liability or supervening cause question in negligence, reduces to the single question of foreseeability. It is clear that an intervening cause will be treated as a supervening cause only if it is unforeseeable to the defendant. *Prosser and Keeton on* [39] *Torts*, § 44 at page 302 (5th ed. 1984).

The foreseeable misuse defense in strict products liability reduces to the same question. Quote:

> "In effect, the question [of foreseeable misuse] is simply whether the intervening alteration of the product was the superseding cause of the injuries." See *Hales vs. Green Colonial, Inc.*, 490 F.2d 1015 at 1020 (8th Cir. 1974)

(90) Admiralty law incorporates the theory of strict products liability and generally applies § 402A of the Restatement Second of Torts. *East River Steamship vs. Transamerica Deleval*, 476 U.S. 858 (1986); *Pan-Alaska Fisheries vs. Marine Construction and Design*, 565 F.2d 1129 (1977). According to the restatement,

> "(1) One who sells any product in a defective condition unreasonably dangerous to the user or consumer or to his property is

subject to liability for physical harm thereby caused to the ultimate user or consumer or to his property if

(a) The seller is engaged in the business of selling such a product, and

(b) It is expected to and does reach the user or consumer without substantial change in the condition in which it is sold.

(2) The rule stated in subsection (1) applies although

[40] (a) The seller has exercised all possible care in the preparation and sale of his product, and

(b) The user or consumer has not bought the product from or entered into any contractual relationship with the seller."

(91) Defendants contend that § 402A of the Restatement does not apply to McDruga's acquisition of the *Saratoga*. They suggest that the rationale of § 402A does not apply to the sale of a large, customized commercial tuna boat between a buyer and seller of comparable economic strength and sophistication in the relevant industry.

(92) In *Chubb Group of Insurance Companies vs. C. F. Murphy & Associates, Inc.*, 656 S.W.2d 766 (Mo.App. 1983), the

court held that the contractor and architect of a large, commercial building could not be held liable under strict products liability but remanded for further development of the facts on a products liability claim against the manufacturer and distributor of allegedly defective steel.

In reviewing the development of § 402A of the Restatement, the court in *Chubb Group* agreed, quote,

> " . . . that in all likelihood the drafters of the restatement did not intend to include real property [41] within the language of 402A."

However, most jurisdictions which have considered the question would include newly constructed homes within the meaning of "product" in products liability law.

(93) In *McKay vs. Rockwell International Corporation*, 704 F.2d 444 (9th Cir. 1983), the Ninth Circuit ruled that a government contractor was not liable under Section 402A under certain limited circumstances. These included that the United States was not liable under the Federal Tort Claims Act, that the United States provided precise specifications for the product, that the equipment conformed to the specifications and that the contractor warned the United States about patent defects in the product. See *McKay* at 451.

While the ruling was based on a Federal Tort Claims Act and government contractor jurisprudence, the court went on to further explain the result by analyzing the policy considerations under Section 402A. The court concluded that the policies did not support strict products liability under the peculiar fact situation presented in *McKay* and that this conclusion reinforced the holding of the court.

(94) I conclude that the real property exception [42] of Restatement § 402A cannot be expanded to apply to tuna vessels or to marine machinery equipment or to hydraulic systems installed on such vessels. The factual similarity to the leading case in the in the Ninth Circuit removes any doubt on this issue. In *Pan-Alaska vs. Marine Construction & Design Company*, 565 F.2d 1129 (9th Cir. 1977), the Ninth Circuit upheld strict products liability for the sinking of the, "76-foot crab fishing vessel, *Enterprise*," based on an oil fire caused by a Caterpillar D343 engine. It would do so in the present case.

(59) MARCO relies on *Snyder vs. ISC Alloys, Ltd.*, 772 F.Supp. 244 (W.D. Pa. 1991) to argue that it should not be liable under the doctrine of strict products liability in the present case. In *Snyder*, defendant ISC signed an exclusive licensing agreement with St. Joe Resources to use St. Joe's patented process for converting zinc metal to zinc dust. St. Joe provided technical service, drawings and plans for the construction of the zinc dust plant. St. Joe did not sell any physical parts to ISC. St. Joe did not have a continuing role in the operation of the plant. The court held that general tort law rather than products liability was the appropriate legal theory.

[43] (96) I conclude that *Snyder* must be distinguished from the present case. The "product" in *Snyder* was entirely the services St. Joe provided to ISC in the building of the plant. St. Joe and ISC did not collaborate to create products to be sold to consumers. Indeed, the court found the lack of any evidence that St. Joe had ever marketed the technology to any other party to be a significant matter. See *Snyder* at 252.

(97) In the present case, MARCO not only designed but advised and tested the hydraulic system during the construction

of the vessel and warranted the performance of the hydraulic system as installed by Martinac Shipyards.

(98) I conclude that MARCO's part in the construction and installation of the hydraulic system of the *Saratoga* goes beyond providing mere service, but MARCO may be considered as the designer and manufacturer of the MARCO hydraulic system.

(99) MARCO also relies upon *Employers Insurance of Wausau vs. Suwannee River Spa Lines*, 866 F.2d 752 (5th Cir. 1989), and *Watson. Watson & Rutland/Architects Inc. vs. Board of Education*, 559 So.2d 168 (Ala. 1990). These [44] cases have to do with contracts for professional services only and do not involve strict products liability.

(100) Respondents contend that, under § 402(4)(1) of the Restatement, the MARCO hydraulic system installed on the *Saratoga* by Martinac Shipyards was not defective. They rely upon comment (g) of Section 402(a), quote:

> "The rule stated in this section applies only when the product is, at the time it leaves the seller's hands, in a condition not contemplated by the ultimate consumer which will be unreasonably dangerous to him."

(101) Respondents say that admiralty cases interpreting § 402A including those of the Ninth Circuit have followed the rationale of comment (g) to 402A and have concluded there is on product defect where the user is aware of the dangerous features of the product. See *Complaint of Diehl*, 610 F.Supp. 223 (D.C. Idaho 1985), and *McCune vs. Aliota Fish Company*, 597 F.2d 1244 (9th Cir. 1979).

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(102) In *Complaint of Diehl*, the District Court applied a consumer expectation test to conclude that an uninsulated, metal main mast on a sailing boat was not a [45] design defect. The boat's mast hit a power line in the harbor causing an explosion and fire which killed most on board. The court held that the danger of running a metal mast into a power line was open and obvious. Quote:

> "A fair reading of Section 402A and its comments reveals that open and obvious dangers inherent in some products do not necessarily make them 'unreasonably dangers'. Rather, only latent dangers, not reasonably discoverable or not contemplated by consumers, render products defective." See *Diehl* at 227.

(103) The Court of Appeals in *McCune vs. Aliota Fish*, 597 F.2d 1244 reviewed findings and conclusions made by the District Court. In its findings, the trial court had found no defect in the winches which were of proximate cause to any of petitioner's injuries.

The court also found that petitioner's injuries were due solely to his own ignorance or of others apart from the respondent, that the manufacturer of the winches had made no warranties, that the uncovered moving parts of the winch in which petitioner caught his foot were open, obvious and apparent to everyone, that the winches were installed in 1971 and no complaints about the winches were made until the time of the accident in 1974.

The Court of Appeals held that, on the District [46] Court's findings, there was no defect in the winches sold by respondent

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which were a proximate cause to petitioner's injury. This finding precluded any recovery under the strict products rationale of Restatement § 402A; that is, the court concluded that the product had been found by the trial judge not to be defective in any way causing petitioners injury.

(104) Contrary to respondent's position, I conclude that there has been considerable criticism of the so-called consumer's expectations test illustrated under comment (g) of Restatement § 402A. A number of courts and legal commentators have adopted the risk/utility analysis in determining whether a product may be dangerous within the strict liability definition of Restatement § 402A.

(105) Legal commentators have also become increasingly critical of a pure application of the consumer expectation test in the development of land-based products liability law. See *Prosser & Keeton on Torts*, 698 (5th ed. 1984).

California and Alaska allow a plaintiff to show a defect under either test. See *Barker vs. Lull Engineering Company*, 20 Cal.3d 413 at 432 (1978); *Caterpillar Tractor Company vs. Beck*, 593 P.2d 871 (Alaska [47] 1979).

(106) The consumer expectations test has been most criticized when the danger can be described as open and obvious. The refusal to find liability for an open and obvious danger is sometimes called the "patent danger bar".

(107) The California Supreme Court has, quote,

> "... flatly rejected the suggestion that recovery in a products liability action should be permitted only if a product is more

> dangerous than contemplated by the average consumer, refusing to permit the low esteem in which the public might hold a dangerous product to diminish the manufacturer's responsibility for injuries caused by that product." *Barker vs. Lull*, 20 Cal.App.3d 425.

On the other hand, the "patent danger bar" has shown a continued vitality in some states, particularly in failure-to-warn cases. See *Grey vs. Manitowoc Company, Inc.*, 771 F.2d 866 at 870 (5th Cir. 1985), applying Mississippi law.

(108) The risk/utility test has been accepted and applied in maritime law. Quote:

> "In different kinds of product cases and without noticeable consistency, admiralty courts have variously applied the risk/utility test, the consumer contemplation test or a hybrid of the two . . . Admiralty decisions reveal that no predictable [48] fact pattern or particular liability theory will dictate application of any one test, so it is not believed possible to identify a consistently preferred admiralty standard." Wanacott, *Products Liabilities of Shipbuilders and Repairers*, 62 Tul.L.Rev. 465 (1988).

(109) In *Pavlides vs. Galveston Yacht Basin, Inc.*, 727 F.2d 330 (5th Cir. 1984), the court applied a risk/utility analysis to determine that the design of the void bilge space and drains on a sport fishing boat was not unreasonably dangerous. When the bilge plug apparently fell out, the boat quickly filled with the

water. The water shorted out the bilge pump, and later the engine battery, so that the boat could not be drained by accelerating the boat. The Fifth Circuit stated that, quote,

> " . . . the determination that a product is unreasonably dangerous . . . means that, on balance, the utility of the product does not outweigh the magnitude of the danger . . . In other words, it must be so dangerous that a reasonable man would not sell the product if he knew the risk involved. See *Pavlides* at 337, quoting *Borel vs. Fibreboard Paper Products Corp.*, 493 F.2d 1076 (5th Cir, 1973), cert. denied, 419 U.S. 869 (1974) (asbestos).

The court went on to find liability based on a failure to adequately warn of the dangers.

[49] (110) I conclude that the claimant in an admiralty case such as now before this Court can show that a product is in a defective condition and unreasonably dangerous under either the consumer expectation test or the risk/utility test. In this case, I conclude that the risk/utility test is most appropriate and should be applied.

(111) I conclude that Saratoga, when constructed, met all requirements of the regulations or the rules and standards of industrial practice followed in the construction of tuna vessels and other commercial vessels.

(112) But despite compliance with the standards and regulations, the MARCO hydraulic system in design

incorporated an unreasonable risk not only to the vessel but to the crew who served aboard her. The placement of the hydraulic hoses carrying combustible hydraulic fluid at operating pressures of 2,000 psi in close proximity to a Caterpillar engine and turbocharger operating at temperatures above the flash point of hydraulic fluid was known to create a serious fire risk.

The practice accepted by the industry at the time was to provide a safety factor of 4 to 1 over [50] operating pressures designed into the system.

(113) Nevertheless, it was known and accepted by MARCO, the designer of the hydraulic system, and by Martinac Shipyards, the builder of tuna and other vessels, that hydraulic hoses can and do fail. But knowing this, nothing was done to minimize the unreasonable risk that, although hydraulic hoses were specified with a safety factor of 4 to 1, a failure or rupture of the hose could lead to a fire in the engine room.

The risk was known and should have been considered and reasonable efforts made to isolate the hydraulic hoses from the high temperatures on the surfaces of the engineer or the turbocharger. As Saveker put it, the design of the hydraulic system was an accident waiting to happen.

(114) In evaluating the risk/benefit, it is necessary to weigh the danger of a product against the utility. Under this test, a product can be said to be defective in the kind of way that makes it unreasonably dangerous if a reasonable person would conclude that the danger, whether foreseeable or not, outweighs the utility of the product.

There are three primary reasons for so [51] concluding, quote:

"(1) The harmful consequences in fact from intended and reasonably foreseeable use as resulting from the way the product was designed and marketed up to the time of Plaintiff's injuries, Plaintiff's injury outweighs the benefits in terms of wants, desires and human needs served by the product.

(2) Although the harmful consequences in fact did not exceed the benefits, alternative products were available to serve the same needs or desires with less risk of harm.

(3) Although the harmful consequences do not outweigh the benefits, there was a feasible way to design the product with less harmful consequences."

Most of the products liability litigation relating to design hazards has been concerned with the feasibility of a safer, alternate design. See *Prosser and Keeton, the Law of Torts*, 5th ed. at 699 and 700.

(115) Photographs and other exhibits have been received into evidence at this trial showing water shields serving the purpose of isolating the hydraulic hoses from the engines and turbocharger.

There's been testimony by the engineers concerning metal shields on at least one tuna vessel.

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[52] (116) When the hydraulic hose ruptured or separated from its coupling to the pump, hydraulic fluid came into contact with the hot surfaces of the turbocharger and immediately ignited. The *Saratoga* was lost but fortunately her crew escaped without injury.

(117) I conclude that the MARCO hydraulic system as designed and installed in the *Saratoga* was unreasonably dangerous and was a contributing cause of the fire which ignited in the upper engine room on January 16, 1986 causing the loss of the vessel and all property aboard her at the time she sank.

(118) I conclude that, taking into consideration the unreasonable risk and the magnitude of that risk, there was a feasible way to design the hydraulic system with less harmful consequences. A metal shield or water shield could have been placed in the design so as to isolate the hydraulic hoses from the hot surfaces of the engine and the turbocharger.

FINDINGS ON COMPARATIVE NEGLIGENCE

(119) Respondent's expert, Grief, enumerated a number of reasons which, in his opinion, caused the hydraulic hose to rupture or to disengage from its coupling [53] on January 16, 1986. Among the possibilities he identified were:

- The system was not operated as designed.
- The wrong hose was installed.
- The hose which failed was defective.
- The hose was in poor condition.

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- The hose was not properly crimped into the coupling.

All of these possible causes of hydraulic hose failure could happen even though the designer or shipbuilder specified in the operating manuals hydraulic hoses with a safety margin of 4 to 1.

(120) If a hazard or risk analysis had been undertaken at the time the hydraulic system was designed, it would have been obvious that a number of the possibilities leading to failure of hydraulic hoses could occur even though the specifications called for in the manuals were followed.

It was also known and conceded that failure of a hydraulic hose designed to contain hydraulic fluid during operations of the hydraulic system at 2,000 psi in close proximity to a diesel engine and turbocharger with surface temperatures in excess of the flash point of hydraulic [54] fluid constitutes a serious risk of fire.

(121) But there are other risks which would also have been obvious had a risk analysis been undertaken by the designer. The risk that larger hydraulic equipment or machinery might be installed in order to speed up fishing operations, thus providing greater opportunity to maximize the catch of fish, the risk arising out of the misuse of the hydraulic system by operating the system in excess of its design limitations should have been considered.

(122) All of these risks that might cause or contribute to cause hydraulic hose failure might have been minimized had the design of the hydraulic system included some means of isolating the hydraulic hoses from the high surface temperatures of the Cat engine and turbocharger.

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(123) There is evidence that at the time the hydraulic system was installed on the *Saratoga* that a water shield or jacket was in place over part of the heated surfaces of the turbocharger. The evidence is sharply conflicting as to whether this water shield or jacket had been removed prior to the fire. Ogilvie testified in his deposition that he thought the shield had been removed. He then said he could not recall if it had been removed, but [55] could have removed it himself.

Lewis Jorge was also equivocal in his testimony about whether the water shield had been removed or not.

(124) The Tillet report indicated the turbocharger was not shielded and the Coast Guard report indicated that the apparent cause of the fire was an unshielded turbocharger. The reports have little probative value in resolving the conflict in the evidence regarding removal of the water shield or jacket on the turbocharger attached to the D333 Cat engine.

The photographs forming enclosure 3 to the Tillet report are of an exhaust manifold water shield group and, according to the Tillet report, was taken from a Caterpillar parts book revision published August 1978. Whether these photographs depict the water shield or jacket on a turbocharger attached to the D333 Cat engine, I have no knowledge.

(125) The equivocal nature of the testimony of Ogilvie and Jorge having to do with removal of the water shield or jacket is so uncertain that I am unable to find it more probable than not that the water shield or jacket had been removed from the turbocharger.

[56] (126) Regardless of other evidence at trial including

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evidence given by Assistant Engineer Jorge, I find that the water shield or jacket installed on the turbocharger at the time the hydraulic system was installed on the *Saratoga* at the shipyard did not cover all exposed heated surfaces on the turbocharger, nor were the heated surfaces of the D333 Cat engine covered by a water shield or otherwise isolated from the nearby hydraulic lines.

(127) I find that the water shield or jacket installed on the turbocharger attached to the D333 Cat, if it were in place, would not have prevented the fire from igniting, taking into account the probable pressures in the hydraulic system at the time the hydraulic hose ruptured or disengaged from the coupling.

At the time Jorge entered the upper engine room, he observed the one-and-one-fourth-inch hydraulic hose pulsating.

(128) A few moments earlier, a hydraulic system failure had occurred and Captain Vargas had complained of inability to control the single winch or to lower the net with the bag of fish to the deck. In view of that hydraulic system failure and the pulsating in the hydraulic hose, I find that any efforts to calculate the pressure at [57] the time the hydraulic hose failed would be unreliable.

(129) Jorge observed hydraulic oil rise to the overhead, fall back on the turbocharger and ignite. The experts have made calculations based on their assumptions concerning pressure on the hydraulic system immediately following the failure of the hydraulic hose. I reject those theoretical calculations and accept Jorge's testimony which on this point I find credible and reliable.

(130) Although claimant's expert, Saveker, expressed his

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opinion that the MARCO hydraulic system was an accident waiting to happen, it also appears that the system operated satisfactorily and safely from the time the *Saratoga* was launched in 1972 until 1984 when Captain Vargas resumed command as captain and undertook to bring the *Saratoga* back to what she once was.

(131) At the time Saratoga Fishing acquired the *Saratoga*, Vargas was well satisfied with the vessel. He had served board the *Saratoga* as captain for McDruga, who owned the vessel from the time she passed her sea trials.

Saratoga Fishing neither asked for any representations or warranties as to fitness and condition of the *Saratoga* nor were any commitments given. Since [58] Vargas in 1984 undertook to rehabilitate the *Saratoga*, she had to have been in poor condition at that time.

(132) The vessel's poor condition was also observed by the engineers who served aboard the vessel after Vargas resumed command in 1984. Chief Engineer Ogilvie went board the *Saratoga* in May 1984. He found the vessel in poor condition, undergoing dockside repairs including the overhaul of the D333 Cat engine.

(133) After dockside repairs on her first trip out, Ogilvie noted a number of problems with the hydraulic system. Valves were leaking, hoses breaking on deck, and Ogilvie concluded that the system was worn out. Assistant Engineer Lewis Jorge came on board the *Saratoga* in July 1985. He observed that the D333 Cat engine overheated and occasionally stalled. He replaced pump cartridges which quickly wore out. He found that, on almost every set, problems were encountered with the hydraulic system.

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(134) In October 1985, Chief Engineer Nielsen replaced Ogilvie while the *Saratoga* was at Ponce, Puerto Rico. When *Saratoga* left, Puerto Rico, she was taken to Panama for work on the hydraulic system. Nielsen became aware of excessive temperatures of the hydraulic fluid. He [59] called Captain Vargas' attention to the manuals for the hydraulic system. Nielsen discussed his concern with the D333 Cat which was overheating, but that problem was deferred by Captain Vargas until, according to Vargas, the *Saratoga*'s next layup in a shipyard.

(135) There were other maintenance problems which were neglected. The remote shutoff for the D333 Cat engine had corroded and become inoperative. Nothing was done to make repairs to the shutoff.

After the fire ignited in the upper engine room, the assistant engineer, Jorge attempted to shut down the engine using the cutoff lever, but flames forced him to abandon the effort before he was able to shut the engine down.

The crew was not trained in fire drills or in fire suppression. The point is not that it would have made a difference once the fire ignited in the upper engine room for the expert testimony establishes that the fire became uncontrollable within minutes.

The significance of the poor condition of the *Saratoga* reveals only that Captain Vargas was more concerned with catching fish than making necessary and urgent modifications or repairs to the hydraulic system on the *Saratoga*.

[60] (136) Chief Engineer Ogilvie was aware almost from the time he came on board the *Saratoga* in May 1984 of the problems in the hydraulic system.

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(137) During fishing operations, the hydraulic system did not purse the net as quickly as Captain Vargas wished. Moreover, the net had been enlarged in order to make the fishing operation more successful. The 100-horsepower electric drive and pump were added to provide more hydraulic flow and power to the power block and winches.

A larger 48-inch power block replaced the 42-inch power block to speed up the pursing operations. Ogilvie inserted larger cartridges in the Vickers pump to increase hydraulic flow and power to the equipment and machinery. This caused the D333 Cat to be overworked and overheated.

(138) The velocity of the flow in the hydraulic system exceeded the velocity for which the system was designed to operate. The temperature of the hydraulic fluid exceeded the temperature the system was designed to operate, and the excessive temperatures caused the viscosity of the hydraulic fluid to decrease with an increase of wear on working parts in the hydraulic system [61] and attached machinery.

(139) Increasing the size of the cartridges in the Vickers pumps, along with the other modifications, did not provide sufficient flow or power to purse the seine as quickly as Captain Vargas wished. Chief Engineer Ogilvie attempted to increase power by raising pressures to the power block and winches from 2,000 psi to 2,400 psi by adjusting relief valves.

All of these modifications were incorporated to provide additional flow and power to the equipment and machinery so that the net could be more rapidly pursed, in order to speed up fishing operation and to enhance fishing opportunities.

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(140) When the *Saratoga* went into the shipyard at Ensenada in 1985, work including sandblasting was done on the hull. Sand or grit found its way into the hydraulic system and caused the pump cartridges to wear out in an abnormally short time. The sand or grit destroys or causes wear to vales, pumps and other machinery with closely fitting working parts.

Sometimes valves will stick and not open. The attempts of the engineers aboard *Saratoga* to remove the sand or grit from the hydraulic system were not completely [62] successful.

The pump cartridges continued to wear out in a short period of time even after efforts were made to purge the system of the sand and grit and continued to wear out rapidly up to the time the Saratoga sailed from Panama January 8th, 1987.

(141) On January 16th, the one-and-one-fourth-inch hydraulic hose which failed, causing the fire in the upper engine room to ignite, was observed by Chief Engineer Nielsen to be leaking or weeping at the coupling. The defect had also been observed by Assistant Engineer Lewis Jorge.

Since the proper tool could not be found aboard the *Saratoga* to make up a replacement hose, arrangements were made by radio with the *Chiriqui II* to have the hose made up on board the *Chiriqui II*. The replacement those was to be delivered to the *Saratoga* when the two vessels met in accordance with arrangements.

Captain Vargas had been informed by Chief Engineer Nielsen of the faulty hose and had to be fully aware of the arrangements with the *Chiriqui II* to provide a hose and to meet with the *Saratoga*.

(142) Although it was obvious that the leaking [63] hose was damaged, the hydraulic system was operated during the set made on January 16th. Captain Vargas and Chief Engineer Nielsen had to know that operating the hydraulic system with a damaged hose could create an unreasonable risk that the hose would fail.

(143) I find that poor maintenance of the hydraulic system, the extensive modifications to the hydraulic system and the use of the hydraulic system known to have a defective hydraulic hose all contributed in some part to cause and bring about the catastrophic fire which ignited in the upper engine room of the *Saratoga* January 16, 1987 and was the precipitating cause of the vessel's loss on the following day.

CONCLUSIONS ON COMPARATIVE FAULT

(144) Strict products liability was originally brought into admiralty suits within the Ninth Circuit in *Pan Alaska Fisheries vs. Marine Construction*, 565 F.2d 1129 (9th Cir. 1977). In that case, the crab fishing vessel, Enterprise was returning to Dutch Harbor, Alaska after a major rebuilding of the vessel in Seattle. The rebuilding included the installation of a new D343 Caterpillar marine diesel engine.

While off Nanaimo, British Columbia, fire broke [64] out in the engine room resulting in the sinking and total loss of the vessel. At trial, the district judge rejected the doctrine of strict liability. The Ninth Circuit reversed, adopting the Restatement of Torts, § 402A as the law of products liability in the circuit for cases arising in admiralty.

(145) Under the doctrine of strict liability, manufacturers,

dealers and retailers are all subject to liability because they are an integral part of the overall producing and marketing enterprise that should bear the cost of injuries arising from defective products.

(146) In *Pan Alaska*, the product defect was an oil filter that Caterpillar knew could crack and spray fuel on a hot engine and that this created an extreme fire hazard. Caterpillar had issued a warning notice to its dealers, but this was held insufficient to insulate Caterpillar from liability in view of the extremely dangerous condition to both life and property from a fuel fire on vessels sailing the high seas.

(147) The Ninth Circuit adopted the rule of comparative negligence to strict product liability citing with approval the rule of *Butaud vs. Suburban Marine*, 555 [65] P.2d 42 (Alaska 1976). Quote:

> "We feel that the public policy reasons for strict product liability do not seem to be incompatible with comparative negligence. The manufacturer is still accountable for all the harm from a defective product except that part caused by the consumer's own conduct." *Butaud*, 555 P.2d at 46.

(148) Having adopted the rule of comparative negligence to strict products liability, the Ninth Circuit addressed the question of what conduct of the plaintiff should be compared. The court answered that question, saying, quote,

> "In short, we hold that all of the Plaintiff's conduct contributing to his loss or injury can

> be compared to the Defendant's liability regardless of the label attached to that conduct."

This ruling marks a significant departure from that part of § 402A of the Restatement which would bar recovery by a plaintiff who voluntarily and unreasonably proceeds to encounter a known risk amounting to assumption of the risk.

In specifically rejecting that provision of Restatement § 402A, the Ninth Circuit ruled, quote:

> "Such 'all or nothing' defenses are inequitable in their operation because they fail to distribute responsibility in proportion to fault and place upon one party the entire [66] burden of a loss for which two are, by hypotheses, responsible."

(149) I conclude the rationale of the Ninth Circuit in *Pan Alaska* is particularly appropriate to the controlling issues in the present case.

(150) The MARCO hydraulic system as installed was delivered to the owner of the *Saratoga* with an unreasonably dangerous defect. Obviously, the hydraulic system operated satisfactorily and safely from 1972 until 1984 when Captain Vargas resumed command of the *Saratoga*.

In the period 1984 until the loss of the *Saratoga* in January 1986, the hydraulic system was not maintained as well as it should have been, but more than that, Captain Vargas wanted to increase the speed and power of the hydraulic system in order to make the most of every fishing opportunity that arose.

(151) In order to accomplish his purpose, Captain Vargas enlarged the net aboard the *Saratoga*, increased the size of the power block, installed an electric drive with pump to supplement the power drive and otherwise called upon the engineers aboard the *Saratoga* to increase velocity of hydraulic flow and power to the machinery and equipment.

[67] The engineers well understood that increased velocity of flow of hydraulic fluid would increase the temperature of the hydraulic fluid causing loss of viscosity in the fluid, thus resulting in more wear and accelerated deterioration of the component parts of the system including hydraulic hoses.

(152) The impact of the increased velocity of flow in the system and the operation of the hydraulic system in excess of design pressures and temperatures brought about increasing failures and malfunction in the operation of the hydraulic system.

(153) Not only were the engineers on *Saratoga* aware of the consequences of operating the hydraulic system beyond its design pressure and temperatures, but they informed Captain Vargas that the hydraulic system was overworked, wearing out and prone to an increasing number of failures.

(154) The conditions causing the hydraulic system to operate in excess of design pressures and temperatures increased the probability of failure in the components in the system including hydraulic hose. More than that, the engineers of the *Saratoga* observed the [68] consequences of misuse of the hydraulic system and the failures, breakdown and wearing out of the system. They informed Captain Vargas of the increasing problems with the hydraulic system, but he continued to operate

the equipment and the machinery of the hydraulic system excess of design pressures and temperatures and to defer needed remedial measures until such time as the *Saratoga* should complete its fishing voyages.

(155) The use of the hydraulic system after the defective one-and-one-quarter-inch hydraulic hose was discovered and known to be damaged and after arrangements had been made with the *Chiriqui II* to provide a replacement border on irresponsible conduct.

Although Chief Engineer Nielsen in his deposition testified he did not consider the defective hose to be dangerous, he had to be aware that it required replacing and that the hydraulic system should not be operated.

Nielsen informed Captain Vargas so that a replacement could be obtained. Nielsen in fact had a great deal of experience and knowledge with hydraulic systems. I do not accept his testim ny that he was unaware of the unreasonable risk of danger created by the defective hose.

[69] (156) Placing the hydraulic system into operation to make a set with a defective hose created an unreasonable and extreme danger that the hose might fail and hydraulic fluid might come in contact with the heated surface of the Cat engine and turbocharger and, of course, that is precisely what happened.

(157) Respondents rely upon *C&S Fuel vs. Clark Equipment*, 552 F.Supp. 340 (E.D. Kentucky 1982). In that case, a tractor shovel was destroyed by fire from hydraulic fluid coming in contact with parts of the engine sufficiently hot to cause ignition. A deflector plate which provided marginal safety

in isolating hydraulic fluid from the hot surfaces of the engine had been substantially changed by a prior owner of the shovel in a way not foreseeable to the manufacture.

The District Court found the design of the shovel defective under strict liability standards. However, the court held any substantial change after the product has left the manufacturer will serve to insulate the manufacturer from liability.

(158) Respondent suggests that removal of the water shield or jacket from the turbocharger attached to the D333 Cat engine amounted to a substantial change [70] insulating Martinac and MARCO from liability.

(159) I have found that the evidence fails to prove that the water jacket or shield on the turbocharger attached to the D333 Cat had been removed prior to January 16, 1986. However, there were substantial changes or modifications to the hydraulic system which I find have contributed in some part to the cause or the failure of the hydraulic hose causing the hydraulic fluid to escape and the ignition of the fire on January 16th.

Moreover, I have found that the hydraulic hose that failed was in a defective condition and known to be defective at the time the hydraulic system was put into operation to make the set in the afternoon of January 16.

The hydraulic system had been operated for some period of time prior to January 16th in excess of design limitations for temperature and pressure. I have found as well that the use of the hydraulic system with the defective hose was a substantial cause of the failure of the hydraulic hose.

(160) So that there will be no doubt of my ruling on the critical legal issue, I reject the rationale of *C&S Fuel vs. Clark Equipment* and of other cases which hold that a substantial change in the product or a [71] substantial change in the use of a product serves to insulate the manufacturer of a product which is defective at the time it leaves the manufacturer.

(161) I read *Pacific Alaska vs. Marine Construction*, the controlling case in the Ninth Circuit, to specifically reject such "all or nothing defenses" because they fail to distribute responsibility in proportion to fault and place upon one party the entire burden of a loss for which two are responsible.

(162) In the present case the MARCO hydraulic system at the time it was installed in the *Saratoga* created an unreasonable risk of fire in the event of failure of the hydraulic hoses. Failure of the hydraulic hoses could have occurred in a number of ways, some of which were identified by respondent's expert, Grief. But hydraulic hose failure was foreseeable not only for the reasons Grief articulated, but for numerous other causes including misuse, poor maintenance and defects of the hose, both apparent and non-apparent.

(163) The failure of the hydraulic which allowed hydraulic fluid to escape and come in contact with hot surfaces on the turbocharger attached to the D33[illegible] Cat was [72] not only caused by the defective design in the MARCO hydraulic system but misuse of the hydraulic system caused by a numb[illegible]of factors.

The modification of the hydraulic system caused it to be operated with temperatures and pressures in excess of design limitations. The hydraulic system was poorly maintained. Sand and grit which entered the system during shipyard repairs had not

been carefully cleaned or removed. The hydraulic system was operated with a defective hose which failed and immediately caused the fire to ignite.

(164) The MARCO hydraulic system, a defective product, was in part responsible because the failed hydraulic hose was in close proximity to the heated surface of the engine and turbocharger, without barriers or shields to isolate the hydraulic fluid from the sources of ignition.

(165) The misuse of the system and negligence of the engineers and the captain of the *Saratoga* were substantial causes of the failure of the hydraulic hose, which allowed the hydraulic fluid to escape and come into contact with hot surfaces which ignited the hydraulic fluid. Sharing the responsibility for the loss in proportion to fault makes sense and I conclude is [73] consistent with the rule of the Ninth Circuit.

(166) The designer and manufacturer of the defective hydraulic system was MARCO, but the system was installed by Martinac Shipyards. Martinac had a duty to provide a safe vessel. Both MARCO and Martinac are liable for the defective product.

(167) In this case I conclude that the greater fault for the catastrophic fire brought about the failure of the hydraulic hose and which ultimately caused the loss of the *Saratoga* and all the property aboard her lies with the engineers and the captain of the vessel.

I conclude that Saratoga Fishing should bear two thirds of the loss of the *Saratoga*, and Martinac Shipbuilding and MARCO Seattle should jointly bear one third of the loss.

That will end the findings and conclusions on liability. It's my intention that, as soon as I can review the issues of law and the evidence on the damages, to enter findings and conclusions on the damage issues.

(Proceedings concluded.)

[74] I certify that the foregoing is a correct transcript from the electronic sound recording of the proceedings in the above-entitled matter.

s/ Mary Lou Lohr — 3-25-93
Transcriber — Date

APPENDIX F — ORAL FINDING ON DAMAGES DELIVERED BY THE DISTRICT COURT ON AUGUST 31, 1993

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF CALIFORNIA

Case No. 87-1691-F

Anchorage, Alaska
Thursday, May 28, 1993
10:48 o'clock a.m.

SARATOGA FISHING COMPANY,

Plaintiff,

vs.

J.M. MARTINAC & COMPANY and MARCO SEATTLE, INC.,

Defendants.

FINDINGS AND CONCLUSIONS ON DAMAGE

TRANSCRIPT OF PROCEEDINGS

BEFORE THE HONORABLE JAMES M. FITZGERALD
UNITED STATES DISTRICT JUDGE

APPEARANCES:

Court Recorder: NATALIE DAY
U.S. District Court
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Appendix F

Transcription Service: KRON ASSOCIATES
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Proceedings recorded by electronic sound recording, transcript produced by transcription service.

[2] ANCHORAGE. ALASKA – THURSDAY. MAY 28. 1993

(On record at 10:48 a.m.)

THE CLERK: On record.

THE COURT: And this is the case, it starts out (indiscernible) and Martinac & Company and others. And these are the findings and conclusions in San Diego. And I'm now putting on the findings on damages. And the format is that each one of the finding — each one of the conclusions will be numbered and there will be a double space, that's the way it's done, and then we order out the conclusions on damages.

And I'll put it on the record, but we will give you a — I'll give you this — my notes so you can take my notes and copy them and just return the original to the chambers.

Conclusion — one of the conclusions, the final conclusion, which has to do with the calculations and the numbers, I'm — can be a — doesn't have to be attached and I'm not going to put it of record, it'll just become part of the conclusions on damages.

THE CLERK: Okay.

Appendix F

THE COURT: To be attached —

THE CLERK: With the transcript.

THE COURT: — at the — when they return the transcript of the conclusions.

I begin. And this is case number 87-1691. It's in the Southern — in the U.S. District Court for the Southern [3] District of California.

On March 18th, 1993, I entered partial findings and conclusions on the liability issues in this case. This order represents the findings and conclusions on damages.

(1) Conclusion 1. I conclude that the proper distinction between the vessel and, quote, "other property," end of quote, under the rule announced in *East River Steamship Corporation vs. Transamerican Deleval*, D-e-l-e-v-a-l, *Incorporated*, 476 U.S. 858, 1986, defines the vessel at the time of the first sale to a commercial customer. A plaintiff may not recover the value of items originally included in the vessel or replacements. Plaintiff may recover the value of other property aboard the Saratoga. *Nicor*, N-i-c-o-r, *Supply Ships Associated vs. General Motors Corporation*, 876 F. 2d. 501, Fifth Circuit 1989.

(2) Conclusion 2. And as I say, there'll be a double space between each of the conclusions. Defendants or respondents concede that the Saratoga was originally sold to Mr. Madrugas, M-a-d-r-u-g-a-s, without a skiff or net. However, respondents argue that the fact that the Saratoga was later sold by Madrugas to Vargas, quote, "as is," end of quote, with a skiff and net requires the conclusion that the skiff and net are now appurtenant

to the vessel under the analogy to maritime lien cases. See *First National Bank & Trust Company vs.* [4] *Oil Screw Olive L. Moore*, 370 F. Supp. 1382, 1973, *affirmed*, 521 F. 2d. 1401, parentheses (Sixth Circuit 1975), end of parentheses.

I disagree for two reasons. First, I conclude that the underlying policy rationale of maritime liens is to give as broad an interpretation of vessel as possible to permit recovery. This rationale is inapplicable to the distinction between the vessel and other property under East River.

Second, I conclude that the definition of the vessel I should change — would change with each successive sale of the boat, including and then excluding the new or removed items on board. This rule of law would be awkward and illogical.

(3) Conclusion 3. Respondents argue that because Vargas, V-a-r-g-a-s, purchased the Saratoga from Madrugas, M-a-d-r-u-g-a-s, with a skiff and net, these items should be defined as part of the vessel, yet seem to indicate that if Vargas had bought the boat in the bare condition one day and the skiff and nets the next, that they would then be, quote, "other property," end of quote, under *East River.*

I conclude that the more rational rule defines the vessel at the time of the original sale to the buyer or — this dovetails with the idea that the existence of a product defect is determined at that time.

[5] (4) Four — Conclusion 4. Plaintiff argues that recovery should be allowed for the replacement parts installed in the Saratoga from the time of its launch — it should be at the time of her launch. Respondents offer authorities holding Section 402,

Subpart A inapplicable under *East River* when replacement parts destroy a product. Citing to *Petroleum Helicopters, Incorporated vs. Avco*, A-v-c-o, *Corporation*, 930 F. 2d. 389, parentheses (Fifth Circuit 1991), end of parentheses; *American Universal Insurance Group vs. General Motors Corporation*, 578 So. 2d. 451, parentheses (Florida Appellate 1991), end of parentheses.

The present case is to some extent the reverse. A separate defect has destroyed the replacement parts. I conclude that these cases teach little about the present case.

(5) Conclusion 5. Nevertheless, I find that — respondents' other arguments compelling. I find and conclude that the plaintiff should not be allowed to recover for replacements to original portions of the vessel. The rule suggested by plaintiff would result in a gradual increase in the liability of the shipbuilder as more of the original components are replaced. In other words, as the performance of the product has less relationship to the conduct of the shipbuilder, the shipbuilder's liability grows. I conclude such a result is inconsistent with *East River* and sound [6] admiralty policy.

(6) Conclusion 6. Respondents claim that each of the crewmembers should make a separate claim against the respondents in product liability to recover for their personal effects. I conclude that plaintiff made a good faith and I reasonable settlement of valid claims and should be allowed to recover for this loss. Respondents cite *East Mississippi Electric Power Association vs. Porcelain Products Company*, 729 F. Supp. 512, parentheses (Southern District Mississippi 1990), end of parentheses, for the proposition that recovery for the settlement of claims is economic damage. Even if this is — were

to be the case, this is not a situation, quote, "when the only injury claimed is economic loss," end of quote, *East River,* 476 U.S. at 876.

I conclude that $21,750 paid to the crew on 6/17/86 was a good faith settlement of claims against the Saratoga for the loss of personal effects and is a proper element of damage in this case.

(7) Conclusion 7. I also conclude that plaintiffs should be allowed to recover for the good faith and reasonable claims for the rescue of the crew. While respondents cite authority for the proposition that under a life salvage theory a rescuer can recovery only against the vessel, Eurypylus, E-[7] u-r-y-p-y-l-u-s, *Limitation*, 1945 A.M.C. 1367, parentheses (Southern District New York 1985), end of parentheses, that same case holds that the rescuer can recover on a quasi-contract theory for performing the maintenance and cure obligations of the vessel's owners. See 1377-80.

(8) Conclusion 8. Original claims made by the Chiriqui, C-h-i-r-i-q-u-i, II for the costs of rescuing the crew totaled over $85,000. These were eventually compromised and settled for $21,282.76. I conclude that the settlement was a reasonable and good faith resolution of claims against the plaintiff arising out of the sinking of the Saratoga. It is a proper element of damages. This expense was incurred by plaintiff on 12/12/86.

That should be Conclusion 8. Did I put down 8 there?

THE CLERK: Yes, Your Honor.

(9) Conclusion 9. Plaintiff's expert witnesses on the fishing industry, Charles Peckham, P-e-c-k h-a-m, of Living

Marine Resources, testified that the yellowfin and skipjack tuna aboard the Saratoga would have a marketable weight of 897 tons and a value of $679,450 at Puerto Rico. Respondents' fisheries expert, Leroy Lester, L-e-s-t-e-r, applied a four-percent reduction for over-estimates and the rejection of unsuitable fish.

[8] I find Mr. Peckham to be a more experienced and credible witness on fisheries matters and adopt his estimate of the weight and value of the fish at Puerto Rico. However, the estimate of the value does not include the fuel costs or Panama Canal toll charges involved in getting the catch to Puerto Rico. I conclude that these costs should be deducted from the value of the tuna catch to accurately determine the amount of the tuna loss. I adopt Mr. Lester's estimates that canal dues would total 27,000 and fuel costs would total $22,142. I reject plaintiff's claim that the canal dues and federal fees — and fuel fees would be, quote, "offset by the additional 103 tons of tuna Saratoga would likely have caught on her way to Puerto Rico," end of quote, as too speculative. Damages for the loss of the fish cargo total $630,308.

(10) Conclusion 10. Marine surveyor Henderson, H-e-n-d-e-r-s-o-n, examined the purse seine net aboard the Saratoga in 1985 and found it to be in good condition. Captain Vargas gave detailed testimony about the characteristics and condition of the net. Plaintiff's expert, Captain Kenneth Franke, F-r-a-n-k-e, relied on these observations of the good condition of the net in estimating the value of the net to be 350,000. Respondents' expert, Mr. Lester, did not rely on personal observations of the net in estimating 132,000 value. I finally conclude Captain Franke's testimony to be [9] more credible. Damages to the net are 350,000.

Mr. Henderson and Captain Vargas testified from personal knowledge that the skiff was in very good condition. Plaintiff's experts, Mr. Henderson and Mr. Franke, agreed on a $95,000 value for the skiff. I find and conclude the testimony of these three witnesses to be more credible than Mr. Lester's estimation of a $50,000 value. Damages for the loss of the skiff are $95,000.

(11) Conclusion 11. Captain Vargas estimated that the safe on board the Saratoga contained $16,000 in cash or money. This testimony was not effectively refuted. I find I and conclude Captain Vargas' testimony on this matter to be credible.

(12) Conclusion 12. Exhibit 357 lists the amount of fuel on board the Saratoga at the time of sinking as 105 gallon — 105,000 gallons. At trial, Captain Vargas claimed a higher amount of fuel. Plaintiff originally claimed a price of 96 cents per gallon for the fuel in Puerto Rico, but testimony at trial indicated the proper price was 86 cents per gallon. I find and conclude that damages for the loss of fuel aboard the Saratoga should be 105,000 at 86 cents per gallon, for a total loss of $90,300.

[10] (13) Finding 13 — or Conclusion 13. There is considerable confusion in the evidence about the types and value of miscellaneous other property on board the Saratoga at the time she was lost, both in the evidence and in the closing memorandums of the parties. Captain Vargas testified about the existence of a great number of particular pieces of equipment aboard the Saratoga and whether each was or was not replacement for original equipment.

Where Captain Vargas is unsure, I find that the plaintiff fails to establish that the loss of the item is recoverable under *East River*. Competing valuations for the equipment were substituted

— submitted by Mr. Franke and Mr. Lester as expert valuation witnesses for the plaintiff and respondents, respectfully — respectively.

Mr. Franke used the replacement cost as the measure of the value of the equipment despite the fact that old equipment was used rather than new. Mr. Lester applied a salvage value. Plaintiffs argue that replacement value is justified because tuna boats cooperated to make a, quote, "market," end of quote, by borrowing equipment and repaying the lending boat by replacing the item or crediting the shoreside account, both of which would be at the full replacement value. While this may be true for individual items on an emergency basis, I do not believe that it represents a reasonable estimation of the value of the equipment lost.

[11] (14) Conclusion 14. I find and conclude that Mr. Lester's use of salvage value more accurately reflects the loss incurred. As previously noted, plaintiff may not recover the value of replacement parts. The value of the skiff, net, fish, and fuel has been separately established. Plaintiff should recover for only five, rather than six, speedboats, one being given to the rescue vessel, and the total value of the speedboats is $12,500. The value of the Mercury engines is $12,907. The total value of all other property established with reasonable certainty to be non-replacement equipment is $14,498. The total value of the miscellaneous other property is, therefore, $39,905. Respondents estimate the total value of the other property as valued by Mr. Lester at $54,130.

(15) Conclusion 15. Plaintiff urges this Court to use the California statutory prejudgment interest rate of 10 percent. I conclude that this would be inappropriate. Plaintiff asserts that

there is no established maritime rule on the rate of prejudgment interest. Under maritime law, the prejudgment interest rate is the most recent 52-week T-bill rate, quote:

> "... unless the trial judge finds, on substantial evidence, that the equities of the particular case require a different rate."

Western Pacific Fisheries. Incorporated vs. SS President Grant, 730 F. 2d. 1280, see 1288 and 89, Ninth Circuit 1984. [12] The Saratoga sank on the morning of January 17th, 1986. The previous day, 52-week treasury bills sold at auction at 7.85 percent. Interest rates peaked in 1989 at about 9.5 percent and fell to about 3.5 percent in early 1993. Even with the benefit of this hindsight knowledge, I find and conclude that 7.85 is a fair interest rate, based on the equities of the case. I find no substantial evidence that this rate would be unfair.

(16) Finding 16. Plaintiff argues that prejudgment interest is awarded in maritime cases as a matter of course. While this is true as a general rule, the District Court has a limited discretion to deny prejudgment interest in peculiar or exceptional cases. The Fifth Circuit has held that a high degree of contributory negligence may be a sufficient reason for a District Court to deny prejudgment interest. *Inland Oil and Transport Company vs. Ark*, A-r-k, dash, *White*, W-h-i-t-e, *Towing Company*, 696 F. 2d. 321, see 328-29, Fifth Circuit 1983.

The Ninth Circuit has indicated but not conclusively established that a high degree of contributory negligence is an insufficient basis for the denial of prejudgment interest. See *Alkmeon*, A-l-k-m-e-o-n, *Naviera*, N-a-v-i-e-r-a, *S.A. vs. M/V Marina*, M-a-r-i-n-a, *L*, 633 F. 2d. 789, at 798 note 12, parentheses (Ninth Circuit 1980), end of parentheses.

[13] I am mindful of the principle that, quote, "prejudgment interest is an element of compensation and not a penalty," end of quote. See at 797. I find and conclude that the resent case is not sufficiently peculiar or exceptional to justify departure from the general rule allowing prejudgment interest in admiralty cases.

Respondents should be taxed prejudgment interest on their proportionate share of the damage from the date of the loss until final judgment is entered in this case at the rate of 7.85 percent.

(17) Conclusion 17 includes the calculations of damages. And finally — and that should be attached to the conclusions. And make a final conclusion that respondents should be taxed interest at the rate of $153.09 per day, starting June 1, 1993. The — I will also direct Saratoga Fishing to present a proposed — present and serve a proposed form of judgment in accordance with my — the findings and conclusions I've made in this case.

THE CLERK: Off record.

(Court recessed at 11:12 a.m.)

END OF PROCEEDINGS

I certify that the foregoing is a correct transcript from the electronic sound recording of the proceedings in the above-entitled matter.

s/ illegible
Notary Public in and for Alaska
My commission expires: 2-18-95

Appendix F

X. Total

	Damage	Defendant Portion	Date of Injury	Interest to 1/1/87	Total to 1/1/87
Tuna	$ 630,308	$ 210,103	1/17/86	$ 15,725	$ 225,828
Net	$ 350,000	$ 116,667	1/17/86	$ 8,732	$ 125,399
Skiff	$ 95,000	$ 31,666	1/17/86	$ 2,370	$ 34,036
Fuel	$ 90,300	$ 30,100	1/17/86	$ 2,253	$ 32,353
Equip.	$ 39,905	$ 13,302	1/17/86	$ 996	$ 14,298
Crew	$ 21,750	$ 7,250	6/17/86	$ 307	$ 7,557
Rescue	$ 21,283	$ 7,094	12/12/86	$ 29	$ 7,123
Cash	$ 16,000	$ 5,333	1/17/86	$ 399	$ 5,732
Total	**$1,264,546**	**$ 421,515**			**$ 452,326**

Appendix F

Total Damage With Prejudgment Interest

1/1/87	—	12/31/87	$ 487,833.59
1/1/88	—	12/31/88	$ 526,128.52
1/1/89	—	12/31/89	$ 567,429.60
1/1/90	—	12/31/90	$ 611,972.82
1/1/91	—	12/31/91	$ 660,012.68
1/1/92	—	12/31/92	$ 711,823.67
1/1/93	—	05/31/93	$ 734,940.38

Defendants should be taxed interest at the rate of $153.09 per day starting June 1, 1993.

Dated June 22, 1993 **s/ James M. Fitzgerald**
JAMES M. FITZGERALD, Senior Judge
United States District Court

No. 95-1764

(2)

Supreme Court, U.S.
FILED
SEP 16 1996
CLERK

In The

Supreme Court of the United States

October Term, 1995

SARATOGA FISHING CO.,

Petitioner,

vs.

J.M. MARTINAC & CO.;
MARCO SEATTLE, INC.,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

RESPONDENTS' BRIEF IN OPPOSITION

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16 pp

THE PARTIES

J. M. Martinac & Co. ("Martinac") is a privately held Washington corporation.

Marco Seattle, Inc. ("Marco") is a Washington corporation wholly owned by Marine Construction & Design Co., Inc., a privately held Washington corporation.

Saratoga Fishing Company, Inc. ("Saratoga"), was a privately held California corporation which has since formally dissolved, but retains the legal authority to litigate this matter under California Corporations Code § 2010.

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OPINIONS BELOW

Trial of this matter was held in the Southern District of California before James M. Fitzgerald, Senior United States District Judge, sitting without a jury. The District Court entered written "Findings on Liability" (Petitioner's Appendix E) and later delivered oral "Findings on Damages" (Petitioner's Appendix F). All parties appealed to the Court of Appeals for the Ninth Circuit.

This matter was argued and submitted at Pasadena, California, on February 8, 1995, before a Ninth Circuit panel composed of Robert R. Beezer and John T. Noonan, Jr., Circuit Judges, and David Alan Ezra, District Judge, sitting by designation.

Upon receipt of the initial decision by the Court of Appeals dated April 26, 1995, affirming the decision of the trial court J. M. Martinac & Co. ("Martinac") and Marco Seattle, Inc., ("Marco") filed a petition for rehearing with suggestion for rehearing *en banc*. The petition for rehearing was granted and the suggestion for rehearing *en banc* was rejected. A first amended decision by the Court of Appeals was filed on August 4, 1995, affirming in part, reversing in part, and remanding the matter to the trial court.

Thereupon Saratoga Fishing Company, ("Saratoga") filed a petition for rehearing and suggestion for rehearing *en banc*. On October 26, 1995, the first amended decision was withdrawn and a second amended decision was filed adding a separate concurring and dissenting opinion by Circuit Judge Noonan. (Petitioner's Appendix B). A formal order denying the petition for rehearing and suggestion for rehearing *en banc* was entered on November 13, 1995.

Saratoga then filed a second petition for rehearing and suggestion for rehearing *en banc* on November 16, 1995. That petition was denied by the Court of Appeals in an Order filed January 30, 1996. (Petitioner's Appendix A).

STATEMENT OF JURISDICTION

All of the parties below, by petition or cross–petition, seek review of the judgment of the Court of Appeals for the Ninth Circuit dated and entered October 26, 1995. A petition for rehearing filed by Saratoga was denied by an order filed January 30, 1996. Cross–petitions for certiorari were filed timely. This Court's jurisdiction is pursuant to 28 U.S.C. § 1254(1). The district court had jurisdiction of this admiralty case under 28 U.S.C. §§ 1333 and 1291.

STATUTORY PROVISIONS

The case involves the general maritime law of the United States. No statutory provisions are directly affected by the issues raised in the cross–petitions.

REASON FOR SUBMISSION OF RESPONSE

The Respondents filed a petition for certiorari (*No. 96-1763*) and the present petitioner filed the present cross–petition for certiorari. By letter dated August 16, 1996, the Clerk requested the respondents file a response to the cross–petition by September 16, 1996.

STATEMENT OF THE CASE

This is a product liability action brought by a commercial fishing enterprise to recover its commercial losses following a shipboard fire and the sinking of a 14 year–old 200 foot steel tuna

seiner custom–built for a professional user who provided significant design input. The product performed safely until its professional user radically changed the product's design. Even then the product did not fail until the user operated the product with a failed component known to need replacement and with knowledge of the likelihood of imminent failure with catastrophic results. When the product failed – predictably – the only injuries were consequential commercial losses.

Martinac built the M/V SARATOGA in 1971 to order for Mr. Joseph Madruga. The M/V SARATOGA was the third in a series of seven multi–million dollar vessels built for Mr. Madruga by Martinac. Mr. Madruga negotiated with Martinac regarding specifications for the ship, selection of the ship's machinery, warranties, and the risk of loss (Petitioner's Appendix E, pp. 118a–119a) Mr. Madruga also selected Marco brand hydraulic machinery which Martinac purchased from Marco. (Petitioner's Appendix B, p. 12a; Petitioner's Appendix E, pp. 118a–120a).

The M/V SARATOGA was delivered in 1972 and captained by Madruga's protégé, Manuel Vargas. In 1974 Madruga sold the M/V SARATOGA to Manual Vargas' corporation, Saratoga Fishing Company. Madruga and Vargas also negotiated the risk of loss and Saratoga purchased the vessel "AS IS" without any warranty. (Petitioner's Appendix B, p. 12a; Petitioner's Appendix E, pp. 124a–122a).

The hydraulic system as designed and installed met well–established marine practice and the design requirements of commercial and naval vessels, including all regulatory requirements and standards accepted and followed in the shipbuilding industry, including those enacted long after her completion. (Petitioner's Appendix B, p. 16a; Petitioner's Appendix E, pp. 124a–127a. 132a).

During the M/V SARATOGA's 14 years of service, her hydraulic system suffered extensive deterioration through lack of maintenance and radical modification for the purpose of significantly increasing power output. These changes materially increased the rate of failure of hydraulic components and the probability of a catastrophic system failure. (Petitioner's Appendix B, p. 13a; Petitioner's Appendix E, pp. 132a–135a).

On January 16, 1986, a few hours prior to the fire, the M/V SARATOGA's chief engineer noticed that one of the 3 major hydraulic supply hoses for the primary hydraulic system was leaking around its fitting. He recognized the need for immediate replacement of the hose and the significant risk of complete failure during operations, (Petitioner's Appendix B, p. 14a), and that if the hose failed, it presented an extreme fire danger. (Petitioner's Appendix E, pp. 140a–141a). The M/V SARATOGA had an available back–up hydraulic drive unit that would have taken about ten minutes to engage and would have by–passed the leaking hose. Nevertheless, the Captain, being fully informed about the leaking hose, elected to commence fishing operations using the primary hydraulic drive without replacing the leaking hose. (Petitioner's Appendix B, p. 14a). This hose failed resulting in the fire and foundering of the vessel.

Despite the commercial setting of this case, the substantial changes to the product by professional users, the open and obvious nature of the claimed defect, and the professional users' complete awareness of the danger presented by their conduct, the trial court found the proximity of hydraulic supply hoses to the diesel engine to be a design flaw, and awarded damages to Saratoga composed of the value of the catch of fish, fuel, net, skiff, fishing equipment, and spare parts aboard the vessel at the time of her loss. This amount was reduced by 2/3 based upon the Saratoga's comparative fault. (Petitioner's Appendix B, p. 16a).

The Ninth Circuit by its amended decision reversed the damages for loss of the skiff, net, fishing equipment and fuel, but affirmed the award as to the value of the lost catch on board at the time of the loss.

DISCUSSION

The parties agree (1) that the present decision places the Ninth Circuit into conflict with the Fifth Circuit; and (2) that the applicable law is confused and uncertain; and (3) a definitive decision from this court would be of immense help to the maritime bar, as well as to maritime insurers, vessel operators, and marine risk managers.

Beyond that, the parties have radically divergent views of the current state of the law, and form which the law should take.

A. There Is An Inter–Circuit Conflict Which Requires Resolution By This Court.

That portion of the Ninth Circuit's opinion affirming the District Court's judgment is predicated upon the cargo aboard the vessel being "other property" and therefore not subject to the limitation on tort recovery imposed by this Court's decision in *East River SS Corp. v. TransAmerica Delavel*, 476 U.S. 858 (1986). Similarly the partial reversal is predicated upon the net, speed boats, skiff and other fishing equipment acquired by Saratoga when it purchased the vessel *not* being "other property."

If Saratoga's expansive view of "other property," derived from an examination of "what–the–defendant–sold" is adopted, then as noted by Circuit Judge Noonan in his dissent, the present case, insofar as it restricts damages recoverable by the plaintiff, is in conflict with the Fifth Circuits decision in *Nicor Supply*

Ships Associates v. General Motors, 876 F.2d 501, 505-506 (5th Cir. 1989). However, if a more restrictive definition of "other property" is used, then the present decision holding that the cargo is "other property" and therefore a recoverable element of damages, is in conflict with the Fifth Circuit's decisions in *Louis Dreyfus Corp. v. 27,956 Long Tons of Corn*, 830 F.2d 1321 (5th Cir. 1987), and *Employers' Ins. of Wassau v. Suwannee River Spa Lines, Inc.*, 866 F.2d 752 (5th Cir. 1989); both of which state, without discussion or explanation, that cargo is not "other property."

Although the present decision pays lip service to the Restatement, it explicitly abandons the "consumer expectation" test set forth in Comment *i* to Restatement (Second), Torts, § 402A, as the touchstone or test for strict product liability and substitutes an alternative, retrospective "risk–utility" analysis at the option of the plaintiff, because as the court admits, application of the § 402A consumer expectation test would preclude recovery. (Petitioners Appendix B at p. 25a). In doing so, it places the Ninth Circuit in conflict with the Fifth,[1] Sixth and Seventh Circuits which accept § 402A as the definitive statement of the maritime law of strict product liability. *Vickers v. Chiles Drilling Co.*, 822 F.2d 535, 538 (5th Cir. 1987); *Miller v. American President Lines, Ltd.*, 989 F.2d 1450, 1462 (6th Cir. 1993); *McKee v. Brunswick Corp.*, 354 F.2d 577, 584 (7th Cir. 1965).

---

1. The Ninth Circuit relies upon *Palvides v. Galvaston Yacht Basin*, 727 F.2d 330, 337 (5th Cir. 1984), for the proposition the risk-utility test applies in admiralty. However, 3 years later in *Vickers, supra*, the Fifth Circuit reaffirmed the proposition that the official comments of § 402A, specifically including comment *i* — the statement of the consumer expectation test — sets forth the test for application of the doctrine of strict products liability. 822 F.2d at 538.

B. There Is Significant Confusion In The Scope Of Damages Available Under The Maritime Law Of Strict Products Liability To The Owner Of A Product Which Destroys Itself.

This case arose out of the murky mush between contract and tort. The maritime law has borrowed the concept of strict product liability in tort from the American Law Institute's Restatement (Second) of the general, land–based, law of torts. It works well in the consumer and personal injury context for which it was designed and which law it "restates."

The maritime law has also borrowed the warranty law codified by the Uniform Commercial Code, to govern the relationship between commercial entities. It, too, works well in the context of commercial relationships. When these conceptually distinct bodies of law occasionally overlap, as in the present case, choices must be made based on overriding public policy concerns, both to promote uniformity and to preserve the role of contract in commercial maritime transactions.

The Petitioner seeks to have this Court define "other property" associated with a commercial transaction in a broad way to permit tort recovery in purely commercial cases. This would mean that every future case would turn on semantics. That is, every frustrated commercial plaintiff who found the contract/warranty remedy inapplicable, would turn to tort, narrowly define the product, claim injury to "other property" and thereby obtain recovery for all identifiable ancillary items appended to or used with the commercial property for which recovery was barred or otherwise unavailable under contract/warranty law.

This case highlights the widely diverse legal interpretations that can be gleaned from the existing body of maritime law

applying strict products liability. The Ninth Circuit's opinion herein only compounds that confusion. This confusion may well stem from the "square peg/round hole" problem posed by trying to apply consumer-based legal principles to purely commercial transactions. The fit is poor, but to the extent the square peg is small enough to fit in the round hole, there are enough discrete spaces left to preclude uniformity.

East River assumed principles of strict product liability can be applied in commercial maritime transactions, but noted the need to significantly limit the application of these principles in a commercial context lest ". . . contract drown in a sea of tort." 476 U.S. at 866. While lower courts and commentators have read a great deal into the *East River* decision, the fact remains that the Court did not define either "*the product itself*" or "*other property*" or the associated concept of "*economic loss*." So, although the Court's message to preserve preeminence of contract law in commercial maritime law was stated clearly, the reluctant implementation of that message has left the law ambiguous and inconsistent. Ten years later, *East River* is widely cited and discussed, with the divergent interpretations of numerous courts, like those of the litigants herein, juxtaposed.

Strict products liability, contract, warranty, the Uniform Commercial Code, and the goal of uniformity in the law are not concepts or legal embodiments unique to maritime law. *East River* is more widely cited by state courts interpreting their own law of strict products liability than by the lower federal courts applying maritime law. The goal of uniformity in maritime law should embrace, wherever possible, uniform land-based principles. Indeed, § 402A is a land-based iteration grafted onto the maritime law, first by the Ninth Circuit in *Pan Alaska Fisheries, Inc. v. Marine Const. & Design Co.*, 565 F.2d 1129 (9th Cir. 1977) and then by this Court in *East River, supra*.

In the ten years since *East River*, strict product liability cases have provided a battleground between those who would expand the concept to make all manufacturers insurers of any losses involving goods they place in the stream of commerce, and those who seek to entirely eliminate the liability of manufacturers for defects in their products. Caught in the middle of this struggle are a multitude of maritime enterprises. The predictable contract-based method of doing business endorsed by *East River* is being eroded, if not gutted, by the Ninth Circuit's expansion of strict product liability law.

It is now of critical importance that this Court decide: (1) what iteration of strict product liability is to be followed by federal maritime law, and (2) which commercial losses, if any, can be recovered under strict products liability under federal maritime law, and which are recoverable only in contract or pursuant to a warranty. The latter question involves preserving the role of contract in commercial maritime intercourse.

What the Ninth Circuit has done is to utilize California's rational extrapolation of strict product liability extending to personally injured consumers a choice of "tests" for a defective product, *Barker v. Lull Engineering Co.*, 20 Cal. 3d 423, 432 (1978), to justify its departure from the consumer expectation test of § 402A. However, the Ninth Circuit failed to recognize that a California court would have denied liability in this case because a California strict products liability remedy is unavailable when commercial parties of relative equal bargaining strength bargain the specifications of a commercial product. *Kaiser Steel Corp. v. Westinghouse Electric Corp.*, 55 Cal. App. 2d 737, 748 (1976). This is a solution suggested by *East River*, 476 U.S. at 871 fn. 6, but not as yet explicitly implemented in the maritime law.

CONCLUSION

The Respondents agree with the Petitioner that the case presents important questions of maritime law which should be settled by this Court for the benefit of the commercial maritime community. However, the Respondents believe the pertinent questions upon which certiorari should be granted are not as set forth by the Petitioner, but rather are:

1. Can a plaintiff state a claim under the admiralty and maritime law of the United States for "strict product liability" when a custom manufactured product fails and only consequential commercial losses are sustained?

2. Does § 402A of the Restatement (Second) Torts provide the definitive statement of the maritime law of "strict product liability" or are other legal regimes also a part of the maritime law?

3. Is lost fish harvest aboard a factory fishing vessel an "economic loss" or "other property" when the vessel destroys itself, *i.e.*, can a tort claim be stated against the manufacturer or is the vessel owner's only potential remedy in warranty?

Marine builders, contractors, subcontractors, and non–maritime companies making occasional sales of goods destined for maritime use, lack a clear definition of their duties and liabilities under existing strict product liability precedent. It is beyond question that strict product liability principles grew out of the need to protect consumers. But, there is no sound public policy basis supporting their application in maritime commerce where contract law provides a more predictable and satisfactory system for adjusting commercial losses.

Marco Seattle, Inc., and J. M. Martinac & Co. therefore pray this Court issue a Writ of Certiorari to review the decision of the United States Court of Appeals for the Ninth Circuit.

Respectfully submitted,

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No. 95-1764

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1996

SARATOGA FISHING CO.,

Petitioner,

vs.

J.M. MARTINAC & CO.; MARCO SEATTLE, INC.,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR PETITIONERS

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PETITION FOR CERTIORARI FILED APRIL 29, 1996
CERTIORARI GRANTED OCTOBER 15, 1996

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QUESTIONS PRESENTED

1. Does the Ninth Circuit's majority opinion on how courts are to determine "other property" in maritime product liability suits conflict with this Court's decision in *East River S.S. Corp. v. Transamerica Delaval Inc.*, 476 U.S. 858 (1986)?

2. Has the Ninth Circuit, by holding that the "product" at issue in maritime product liability suits is the ship as sold, not by the manufacturer, but by the last person who owned the ship, abrogated the well established law of maritime products liability set forth in *East River*, and the decisions of other courts, including the Fifth Circuit's opinion in *Nicor Supply Ships Associates v. General Motors*, 876 F.2d 501 (5th Cir. 1989)?

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CORPORATE DISCLOSURE

Petitioner SARATOGA FISHING CO. has no parent company or subsidiaries.

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I. OPINIONS BELOW

The opinion of the Ninth Circuit Court of Appeals, filed October 26, 1995 (Appendix[1/] ("App."), 4a), is reported at 69 F.3d 1432 (9th Cir. 1995). Neither the district court's Findings on Liability (App., 114a), nor its Oral Findings on Damages (App., 173a) are reported. The original opinion of the Ninth Circuit Court of Appeals, filed April 25, 1995 (App., 80a), and the first revised opinion of the Ninth Circuit Court of Appeals, filed August 4, 1995 (App., 43a) are not published.

II. JURISDICTION

The Ninth Circuit Court of Appeals entered its order denying rehearing of SARATOGA FISHING's ("SARATOGA") motion for reconsideration on January 30, 1996. App., 1a. SARATOGA filed its Petition for Writ of Certiorari on April 29, 1996. This Court granted SARATOGA's Petition for Writ of Certiorari on October 15, 1996. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1). Because these claims arose on the high seas, they fall within the admiralty jurisdiction of the federal courts under 28 U.S.C. § 1333.

1/ All "Appendix" or "App." citations are to the appendices to Appellant SARATOGA's Petition for Writ of Certiorari. Pursuant to Supreme Court Rule 26(1), these appendices were not reprinted.

III. STATEMENT OF THE CASE

A. The Nature of the Controversy

Petitioner SARATOGA sued Respondents for damages resulting from a conflagration that occurred on board M/V SARATOGA on or about January 16, 1986, in which M/V SARATOGA burned and sank. M/V SARATOGA was originally purchased in or about 1972 from the manufacturer, J.M. MARTINAC & CO. ("MARTINAC"), by Joseph Madruga, a private individual. The hydraulic system on the vessel was designed by MARCO SEATTLE INC. ("MARCO"). The vessel was completed in 1972, taken to Panama and outfitted with a seine and other fishing equipment, and Madruga began fishing operations with the vessel, with Manual Vargas as its captain.

In 1974, Joseph Madruga sold M/V SARATOGA to the Manual S. Vargas, Jr. Corporation, which later changed its name to SARATOGA. At the time of that sale, M/V SARATOGA was equipped with five speedboats, fuel, a purse skiff, a seine, and various electronic equipment. On or about January 16,1986, a hydraulic hose detached from its coupling, spraying hydraulic fluid onto the turbocharger. Because MARTINAC and MARCO had failed to provide any effective shielding, the hydraulic fluid sprayed onto the adjacent engine surfaces and turbocharger and ignited. The resulting conflagration burned and sank M/V SARATOGA. The crew just managed to get off the ship

into the skiff before the vessel sank.

B. Proceedings Below

1. The Decision of the District Court

The district court concluded that MARCO and MARTINAC were strictly liable for the loss of M/V SARATOGA in that the hydraulic system was defectively designed. The court awarded damages to SARATOGA in the amount of $452,326, approximately one-third of what it determined were the total of SARATOGA's damages (the total damage award was reduced by two thirds for comparative negligence). The district court's award included the loss of "other property" on board M/V SARATOGA, including the tuna catch, seine, skiff, fuel, equipment, payments by SARATOGA to the crew for their personal property losses, the cost of rescue and certain cash carried on board. This "other property" was property that was *not* part of the vessel at the time it was sold by MARTINAC, the vessel manufacturer, to Madruga, the original purchaser. With pre-judgment interest, the total award to SARATOGA came to $734,940.38.

2. The Ninth Circuit's Original Opinion

All parties appealed the district court's decision on various grounds, only one of which, the determination of "other property," is at issue in this Appeal. In its original opinion, issued April 25, 1995 (the "Original Opinion") (App., 80a), the Ninth Circuit correctly recognized that the "product" in products liability cases, including maritime

products liability cases, is determined by what the *manufacturer* places in the stream of commerce. The Ninth Circuit therefore agreed with the Fifth Circuit that,

> additions to a vessel should be considered other property "separate from the product that the **manufacturer** *originally* sold, if the distinction enunciated in *East River* between a 'product' and 'other property' is to have any meaning."

App., 108a, *quoting Nicor Supply Ships Associates v. General Motors*, (hereafter, "*Nicor*") 876 F.2d 501, 506 (5th Cir. 1989) (emphasis added, italics in the original). To distinguish the "product" from "other property" on M/V SARATOGA, the court looked to "the vessel that MARTINAC sold to Madruga in 1972." App., 108a. To include the items that were not part of the vessel originally sold by MARTINAC to Madruga,

> would undermine the 'other property' exception contained in *East River*. Under that rationale, the product would envelop everything else useful in the operation of the vessel, which is not consistent with the balance struck by the Supreme Court.

App., 108a. MARTINAC and MARCO then moved for reconsideration.

3. The Ninth Circuit's First Revised Opinion

On August 4, 1995 (the "First Revised Opinion")

(App., 43a), the same three-member panel (Beezer, J., Ezra, J. and Noonan, J.) scuttled its well-reasoned Original Opinion and changed course 180 degrees. Misreading *East River v. Transamerica Delaval*, 476 U.S. 858 (1986), the panel unanimously held that the manufacturer's "product" is defined for strict products liability as the object that was last transferred from *any* seller to a buyer, even if the seller, as in this case, is a private person and *not* a "seller...who is engaged in the business of selling such a product" as defined by the Restatement (Second) of Torts, Section 402(1)(a). App., 72a-73a.

SARATOGA moved for reconsideration of the panel's First Revised Opinion, noting that the court's ruling abandoned Section 402A of the Restatement (Second) of Torts, ignored the Ninth Circuit's earlier decision in *Pan-Alaska Fisheries, Inc. v. Marine Construction & Design Co.*, 565 F.2d 1129 (9th Cir. 1977) (adopting Section 402A as the law of the Ninth Circuit), placed the Ninth Circuit in direct conflict with the Fifth Circuit by disregarding the well established maritime rule set forth by the Fifth Circuit in *Nicor*, 876 F.2d 501 (5th Cir. 1989) and misread and placed the Ninth Circuit in conflict with this Court's seminal decision in *East River*.

4. The Ninth Circuit's Second Revised (Final) Opinion and Judge Noonan's Dissent

On October 26, 1995, the winds shifted again and a second revised opinion was issued (the "Final Opinion"). App., 4a. It is from this opinion that SARATOGA appeals. In the Final Opinion, only two members of the

panel, Judges Beezer and Ezra (the "majority"), voted to stand by their First Revised Opinion of August 4, 1995. The third member, Judge Noonan, parted company with the majority on its determination of "other property," recognizing that its decision conflicted with the Ninth Circuit's previous decision in *Pan-Alaska*, placed the Ninth Circuit in direct conflict with the Fifth Circuit's decision in *Nicor*, and placed the Ninth Circuit in conflict with this Court's decision in *East River* as well. App., 40a-41a. Judge Noonan's concurrence and dissent, set forth in full, encapsulates perfectly the Ninth Circuit's error and crystalizes the conflict between the circuits created by the Ninth Circuit's opinion and the Ninth Circuit's departure from the rationale and rule of *East River*:

> I concur in the opinion of the court, except as to its exclusion of damages for the skiff, seine net, fuel, spare parts and other miscellaneous equipment sold by Madruga to Saratoga Fishing as part of the sale of the M/V SARATOGA. None of this property was manufactured or sold by Martinac. Under *East River*, 476 U.S. 858, 867 all of it was 'other property,' damages for which are recoverable in tort. The court abandons *East River* and puts this circuit in conflict with another major maritime circuit, *Nicor Supply Ships Associates v. General Motors*, 876 F.2d 501, 505-06 (5th Cir. 1989). The opinion also repudiates controlling authority in this circuit, *Pan-Alaska Fisheries, Inc. v. Marine Construction & Design Co.*, 565 F.2d 1129 (9th Cir. 1977). That case

> accepted 'as the law of products liability in this circuit, at least for this case arising in admiralty,' the Restatement (Second) of Torts, § 402A *Id.* at 1135. Under the Restatement, the original seller of the product in a defective condition that is unreasonably dangerous that has entered the stream of commerce is strictly liable to the ultimate consumer for physical harm caused to that consumer's property. Saratoga Fishing is here the ultimate consumer; Martinac is the original seller; the property damaged was Saratoga Fishing's and no more part of the product sold by Martinac than was the tuna catch for which damages are granted.
>
> The court appears to have been swayed by the consideration that additions made by a middleman could increase the original seller's liability. That of course is a risk the seller of an unreasonably dangerous, defective product takes. If the explosion had occurred while Madruga still owned the boat after adding the skiff and net, there is no doubt that Martinac would have been liable for those additional items. Martinac's exposure should not decrease because Madruga sold the ship to Saratoga Fishing. Whatever theory one adopts, the liability of the original seller may change as the ultimate consumer adds or subtracts property which can be affected by the defective product. The theory of strict

> liability holds that the seller is stuck whatever foreseeable damage to the consumer's other property his product causes.

App., 40a-41a, Noonan, J., concurring and dissenting.

IV. SUMMARY OF ARGUMENT

The Ninth Circuit erred when it held that for purposes of maritime products liability, a vessel manufacturer's "product" includes all property on board the vessel at the time the vessel is sold by the original purchaser to a second purchaser, whether or not that "other property" was part of the vessel sold by the manufacturer to the original purchaser. The Ninth Circuit erred by misreading *East River* to import a contract (i.e., warranty) analysis into product liability law. *East River* delineated the "sphere" of warranty law to include damages caused by the product to itself and other business-related damages (e.g., lost profits) that might occur where a product breaks down or fails to perform as expected ("economic damages"). However, where the product defect resulted in destruction of property other than the product itself (i.e., "other property"), tort liability (i.e., products liability) was triggered. By misreading *East River* and improperly importing a warranty analysis into products liability law, the Ninth Circuit effectively barred subsequent purchasers of the vessel manufacturer's product from recovering for damages to property that was on board the vessel at the time of purchase, but that was *not* part of the vessel (the "product") placed into the stream of commerce and sold by the manufacturer.

V. ARGUMENT

A. The Ninth Circuit's Ruling Has Created a Conflict in the Circuits, and is in Direct Conflict with this Court's Decision in *East River*

The Ninth Circuit is a major maritime law court. Its October 26 Final Opinion will, if given effect, disrupt maritime products liability law in not only the Ninth Circuit, but in the United States as a whole. By misreading and misapplying *East River*, the Ninth Circuit has decided an important question of maritime law "in a way that conflicts with relevant decisions of this Court." Sup. Ct. R. 10(c). By its error, the Ninth Circuit has in fact disrupted the careful delineation between the "separate spheres" of products liability and contract law set forth by this Court in *East River*. 476 U.S. at 870-871. Moreover, the Ninth Circuit has "entered a decision in conflict with the decision of another United States court of appeals on the same important matter," namely, the Fifth Circuit's ruling in *Nicor* and other decisions. Sup. Ct. R. 10(a).

The Ninth Circuit's erroneous decision creates an intolerable situation that will effectively destroy claims for "other property" by second and subsequent purchasers of a vessel, even though the damage to other property was caused by exactly the same defect that existed at the time the manufacturer sold the vessel to the first purchaser. Effectively, once a vessel is sold or transferred by the first buyer, the second vessel buyer has no remedy for product defects that cause damage to "other property" added to the vessel by the first buyer. Resales or transfers of vessels to

another owner or operator are, however, commonplace, and often occur within a short time of the useful life of the vessel. It is also common that, as in this case, after a vessel is purchased, other items are added to outfit it for its particular purpose. These additional items, as can be seen in this case, can amount to as much or more than one-third of the total value of the vessel.

B. The Ninth Circuit Erred by Misunderstanding *East River's* Clear Delineation Between the Spheres of "Economic Loss," Governed by Warranty and Contract Law, and Non-Economic Loss, Governed by Tort Law

The Ninth Circuit erred by misunderstanding and misreading *East River*'s distinction between the sphere of warranty law, which governs damage to the product itself or consequential losses (e.g., lost profits) suffered because of the failure of the product ("economic loss"), and the sphere of tort law (i.e., products liability law), which governs damage to persons or property *other than* the product itself ("non-economic loss"). It was precisely this delineation that was at issue in *East River*. At the time *East River* was decided, at least two views existed nationwide as to the proper scope of recoverable damages in products liability law. One group of courts, including the California Supreme Court in *Seely v. White Motor Co.*, 63 Cal.2d 9, 45 Cal. Rptr. 17, 403 P.2d 145 (1965), left to warranty law damage caused by the product to itself (i.e., economic loss), leaving to tort law damage caused to property (or to persons) that was *not* part of the product

itself ("other property"). *East River*, 476 U.S. at 869. Another group of courts allowed product liability law to extend not only to "other property," but to the product itself. That is, these courts allowed recovery in tort for "economic damages." *East River*, 476 U.S. at 869. At issue in *East River* was whether bareboat charterers of a vessel could recover in tort from Transamerica Delaval, Inc. ("Delaval"), the manufacturer of the ship's turbines, for damage to the turbines caused by defective turbine component parts. *East River*, 476 U.S. at 860, 875.[2/] As stated by the Court, "we must decide whether a cause of action in tort is stated when a defective product purchased in a commercial transaction malfunctions, injuring only the product itself and causing purely economic loss." *East River*, 476 U.S. at 860.

East River sided with the "majority view" expressed by *Seely*. Warranty law would govern the extent to which a purchaser could recover from the manufacturer for damage to the product itself ("economic damages"), and products liability law would govern recovery for damage to "other property." The logic of the Court was straightforward: If a manufacturer warranted that its product would continue to function properly for a certain

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2/ The bareboat charterer's second amended complaint alleged five counts, the first four of which the Court read as alleging strict liability against Delaval for product defects. The fifth cause of action alleged negligent supervision of the installation of a valve on the ship. The plaintiffs' original complaint had alleged breach of contract and warranty against Seatrain Shipbuilding Corp. ("Shipbuilding") and its parent corporation, Seatrain Lines, Inc. ("Seatrain"). Shipbuilding built the ships. Those claims were dropped in the second amended complaint.

period of time, e.g., 5 years, it could estimate the cost of that warranty and could include that cost in the price it charged for its product. If, on the other hand, the manufacturer offered a short warranty, or no warranty at all, the price it could charge would be less. By offering a short warranty, or no warranty at all, the manufacturer could limit its liability to the purchaser for the failed product (and, similarly, for any economic consequences caused by the failure of its product (e.g., lost business)). The trade-off was that the manufacturer could not charge as much for its product. *East River* recognized that this "price/limitation-of-damages" tradeoff that is the fundamental basis of warranty law was appropriate for those situations in which the product destroyed itself. Products liability law, however, governed where the product defect resulted in injury to a person or property other than the product itself. *See East River*, 476 U.S. at 871, 872.

C. By Misreading *East River* to Import Contract Analysis into Products Liability Tort Law, the Ninth Circuit Erred in Deciding How "Other Property" Is Determined

The panel's Original Opinion correctly recognized that *East River* defined the "product" for products liability purposes is that which the *manufacturer* places in the stream of commerce. The Original Opinion correctly held that the distinction between the "product" and "other property" turned on whether the property was "'separate from the product that the **manufacturer** *originally* sold" to the first buyer; in this case, what MARTINAC sold to

Joseph Madruga, the original buyer of M/V SARATOGA. App., 108a (emphasis added, italics in the original), *citing Nicor*, 876 F.2d at 506. The panel's Final Opinion (and its First Revised Opinion) misread *East River* as holding that the "product" is defined for strict products liability as the object that was last transferred from *any* seller to a buyer, even if the seller, as in this case, is an occasional seller; that is, *not* a "seller...who is engaged in the business of selling such a product" as defined by the Restatement (Second) of Torts, Section 402(1)(a). App., 33a-35a.

The Final Opinion abrogates fundamental products liability principles which provide that 1) only commercial sellers (e.g., manufacturers and distributors), not end-users of a product can be held liable for a product's defects; 2) the "product" at issue in strict products liability analysis is the product the manufacturer or distributor placed into the stream of commerce; 3) product liability cannot be disclaimed by warranty; and 4) "[t]he consumer's cause of action does not depend upon the validity of his contract with the person from whom he acquires the product . . . ." Restatement (Second) of Torts, § 402A, cmt. m (1977).

The Ninth Circuit interpreted *East River* to hold that a downstream sales contract between consumers determines "the product" at issue for purposes of distinguishing "the product" from "other property." App., 33a-35a. The Ninth Circuit was wrong. Looking to a downstream contract to define a manufacturer's "product" for strict products liability purposes ignores *East River*'s determination that the recovery of property damages under maritime products liability law, including strict products liability, is controlled by Section 402A of the Restatement (Second) of Torts. *East River*, 476 U.S. at 875, *citing with*

approval Pan-Alaska Fisheries, Inc., 565 F.2d 1129, 1135 (9th Cir. 1977) (adopting Restatement (Second) of Torts § 402A (1965)).

1. Strict Products Liability Law Applies Only to Sales by Commercial Manufacturers, Distributors or Retailers to Consumers

The Ninth Circuit initially erred when it framed the question before it as "*whether the 'product' changed* when Madruga added various components, including a skiff, seine and other miscellaneous parts, to the vessel and resold it to Saratoga Fishing." App., 33a-34a (emphasis added). By answering "yes," the Ninth Circuit placed Joseph Madruga, a consumer, in the shoes of MARTINAC, the designer and manufacturer of M/V SARATOGA, for purposes of determining MARTINAC's "product."

Section 402A of the Restatement (Second) of Torts, cited with approval by this Court in *East River* and adopted by the Ninth Circuit in *Pan-Alaska Fisheries, Inc.*, 565 F.2d at 1134-1135, provides:

> § 402 A. Special Liability of Seller of Product for Physical Harm to User or Consumer.
>
> (1) One who *sells* any product in a defective condition unreasonably dangerous *to the user or consumer or to his property* is subject to liability for physical harm thereby caused to the *ultimate* user or consumer, or to his property, if
>
> (a) the seller is *engaged in the business of selling such a product*, and
>
> (b) it is expected to and does reach the user or consumer without substantial change in the condition in which it is sold.
>
> (2) The rule stated in Subsection (1) applies although
>
> (a) the seller has exercised all possible care in the preparation and sale of his product, and
>
> (b) *the user or consumer has not bought the product from or entered into any contractual relation with the seller.*

Restatement (Second) of Torts, § 402A (1977) (emphasis added).

A "seller" of a product under Section 402A is unequivocally *not* a consumer reselling the product, but a *commercial* seller (e.g., a manufacturer, distributor) of that product:

> The rule stated in this Section applies to any person engaged in the business of selling products for use or consumption. It

> therefore applies to any *manufacturer* of such product, to any *wholesale or retail dealer or distributor*, and to the operator of a restaurant.

Restatement (Second) of Torts, § 402A, cmt. f (1977) (emphasis added). A "product," as defined by the most recent Tentative Draft of the Restatement (Third) is not an item resold by one consumer to another consumer but,

> something *distributed commercially* for use or consumption. Most but not necessarily all products are tangible personal property; most have been subjected to processing and fabricating prior to entering the stream of commerce; and most pass through a commercial chain of distribution before ultimate use and consumption.

Restatement (Third) of Torts: Products Liability, § 4 (Tentative Draft No. 2, March 13, 1995) (emphasis added).

Joseph Madruga was not in the business of selling tuna boats. Madruga was a small shipowner who sold his boat to his former captain. App., 6a. He was *not* a commercial seller when he sold M/V SARATOGA. He therefore could *not*, by definition, have placed MARTINAC's product into the stream of commerce as a seller under Section 402A of the Restatement.

2. The Ninth Circuit's Final Opinion Undermines the Rationale for Applying Strict Products Liability Only to Commercial Manufacturers and Distributors

The rationale for strict products liability, embodied in *East River*, the Restatement, and the Ninth Circuit's Original Opinion, is the *manufacturer's* ability to spread the risk of defects and to correct defects in the product:

> [T]he justification for the strict liability has been said to be that the seller, *by marketing his product for use and consumption*, has undertaken and assumed a special responsibility toward any member of *the consuming public* who may be injured by it; that the *public* has the right to and does expect, in the case of products which it needs and for which it is forced to rely upon the seller, that reputable sellers will stand behind their goods; that public policy demands that the burden of accidental injuries caused by products intended for consumption *be placed upon those who market them*, and be *treated as a cost of production* against which liability insurance can be obtained; and that the consumer of such products is entitled to the maximum of protection at the hands of someone, and the proper person to afford it are *those who market the products*.

Restatement (Second) of Torts, § 402A, cmt. c (1977) (emphasis added). This Court in *East River* likewise understood that this rationale applied to the *manufacturer*, not the occasional downstream seller:

> The *manufacturer* is liable whether or not it is negligent because 'public policy demands that responsibility be fixed wherever it will most effectively reduce the hazards to life and health inherent in defective products *that reach the market*.' *Escola v. Coca Cola Bottling Co. of Fresno*, 24 Cal.2d, at 462, 150 P.2d, at 441 (opinion concurring in judgment).

East River, 476 U.S. at 866-867 (emphasis added).

East River understood that a manufacturer's strict liability for defective products stands separate and apart from contract based warranty law and is based on a separate rationale:

> Products liability grew out of a public policy judgment that people need more protection from dangerous products than is afforded by the law of warranty. *See Seely v. White Motor Co.*, 63 Cal.2d 9, 15, 45 Cal. Rptr. 17, 21, 403 P.2d 145, 149 (1965).

East River, 476 U.S. at 866.[3/]

[3/] Again siding with *Seely*, *East River* recognized that damage to property did not differ from damage to persons in strict products liability: "For similar reasons of safety, the *manufacturer's* duty of care was broadened to include protection against property damage. [citations omitted] Such damage is considered so akin to personal injury that the two are treated alike. *See Seely*, 63 Cal.2d at 19, 45 Cal. Rptr., at 24, 403 P.2d, at 152." *East River*, 476 U.S. at 867.

Under the Ninth Circuit's reasoning, an occasional seller like Joseph Madruga cannot be held liable under products liability law for a products' defects, and none of the rationales upon which strict product liability rests apply to him. Yet the Ninth Circuit's conclusion is that this same occasional seller can nonetheless "change" the manufacturer's "product" for products liability purposes. App., 34a-35a. The focus of the Ninth Circuit's flawed inquiry was not on what the manufacturer placed into the stream of commerce, but on what the downstream consumer, Madruga, resold. App., 34a-35a. The district court (and the dissent) correctly rejected this awkward result: "I conclude that the definition of the vessel . . . would change with each successive sale of the boat, including and then excluding the new or removed items on board. This rule of law would be awkward and illogical." App., 176a; *see also* App., 41a, Noonan, J., concurring and dissenting.

3. The Ninth Circuit Misunderstood That in *East River*, this Court First Determined That Products Liability Law Did Not Apply Before Going on to Reach a Decision under Warranty Law

The Ninth Circuit claimed that *East River* "focused on the terms of 'the charterers' agreements with the

owners." App., 34a. The Ninth Circuit claimed that "the contract being discussed" throughout *East River* was the contract "between the first buyer and the bareboat charterer, who the court treated as equivalent to a second buyer." App., 34a-35a. The Ninth Circuit was wrong. It misunderstood whom the "buyer" was that this Court was referring to in *East River* when, in the first part of its decision, this Court performed its products liability analysis to determine the identity of the "product" at issue. Like *Shipco 2295, Inc. v. Avondale Shipyards, Inc.*, 825 F.2d 925 (5th Cir. 1987), *East River* focused on the "product" from the perspective of the *first* purchaser, the boat owners[4], not the bareboat charterers.[5] *East River* did

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[4] The owners were subsidiaries of Seatrain. The ships had been constructed under contract between these subsidiaries of Seatrain and another Seatrain subsidiary, Shipbuilding. Shipbuilding had, in turn, contracted the design and manufacture of the ships to Delaval. Finally, the bareboat charterers of the ships were also Seatrain subsidiaries. *East River*, 476 U.S. at 859-860.

[5] The Ninth Circuit may well also have misapprehended the teaching of *Shipco* and its application to this case. After this Court decided in *East River* that recovery in tort was not available where a component part of a vessel injured only itself, *Id.*, 476 U.S. at 871, *Shipco* faced the next question. That is, could a component part manufacturer be held liable in tort for damage to the rest of the vessel caused by the defective component part? The Fifth Circuit answered "no," at least insofar as the component part (e.g, the defective steering gear) had been sold to the original purchaser as an integral part of the completed vessel. *Shipco*, 825 F.2d at 929-930. The focus of *Shipco* was identification of the final, completed product the first purchaser bought from the manufacturer. That case has no bearing where, as here, the sale was a downstream sale between two private parties.

not focus on the downstream agreement between the owners of the vessels and the "second buyers," the bareboat charterers, *until after it had determined that strict products liability law did not apply.*

Thus, in the first part of its decision, *East River* held that the plaintiffs had no products liability claims because *only* "economic damage," that is, damage to the product itself, was at issue. *East River*, 476 U.S. at 867. It made this determination only *after* it had decided what "the product" at issue was. To do this, the Court looked to what had been "*supplied by Delaval*," the manufacturer, to the owners of the ships at the time of delivery to the owners. Because "each turbine was *supplied by Delaval* [the manufacturer] as an integrated package," each turbine was "properly regarded as a single unit." *East River*, 476 U.S. at 867. As a result, because the "defectively designed turbine components [had] damaged only the turbine itself," "*there was no damage to 'other' property.*" *East River*, 476 U.S. at 867.

Once the Court had determined that the turbines were "the product" sold by Delaval to the owners, and that the turbines had damaged only themselves, the Court considered whether damage caused by the product to itself was recoverable in tort under a products liability theory. The Court examined the schism between those courts that held that damage to the product itself was recoverable, and those that did not. *East River*, 476 U.S. at 868-871. Ultimately, the Court endorsed California's Supreme Court decision in *Seely* and held that damage to the product itself (e.g., the turbine supplied by Delaval), was "economic damage" that could not be recovered in tort under a products liability theory. Therefore, such damage

could not be recovered in tort by *either* the owners or the bareboat charterers. *East River*, 476 U.S. at 867, 875. The Court therefore proceeded to its analysis under warranty law.

4. The Ninth Circuit Confused *East River*'s Discussion of Warranty Law with *East River's* Discussion of Products Liability Law

Because it confused *East River*'s discussion of products liability law with its discussion of warranty law, the Ninth Circuit erroneously imported *East River*'s discussion of warranty law into its analysis of SARATOGA's product liability claims. As a result, the Ninth Circuit misunderstood this Court's discussion of "the benefit of the bargain" under warranty law and erroneously applied that discussion to its products liability analysis. The Ninth Circuit's error is seen in the phrasing of its question:

> We must decide whether the "product" changed when Madruga added various components, including a skiff, seine and other miscellaneous parts, to the vessel and resold it to Saratoga Fishing.

> We are guided by the policies set forth in *East River*, where the Court stated that *the focus of the product* should be on the failure of the purchaser to receive the *benefit of its bargain*. Warranty and contract law are appropriate for this type of situation. Here, the purchaser is Saratoga Fishing and the object of its bargain was the M/V SARATOGA with the components already installed. Saratoga Fishing purchased the vessel "as is." Madruga made no "warranty or representation of vessel condition."

App., 34a.

The Ninth Circuit missed this Court's point. The "benefit of the bargain" and "as is" language in *East River* relied on by the Ninth Circuit, App., 34a, played no part in *East River*'s products liability analysis; rather, that language was only relevant to determine whether the bareboat charterers (the subsequent "purchasers" of the vessel) had any remedy in warranty. This warranty analysis came only *after* this Court had decided that products liability law did not apply because the product, the turbines, had only injured themselves. *East River*, 476 U.S. at 867. This Court determined that the bareboat charterers did not have any remedy *in warranty*. No warranties were available because there were no warranties given by the *owners* to the bareboat charterers. The bareboat charterers did not have standing to sue on the manufacturer's warranties to the owners because those warranties had *not* been transferred to the bareboat charterers by the owners. *East River*, 476 U.S. at 875. At

this point, this Court determined that, *under contract law*, there was "no reason to extricate the parties from their bargain." *East River*, 476 U.S. at 875. None of this discussion, contrary to the Ninth Circuit's reading, had anything to do with this Court's products liability analysis in *East River*.

5. East River Understood That "Economic Loss" Did Not Include Damage to Property Physically Separate From the Defective Product

The Ninth Circuit misunderstood what this Court meant by "economic loss" in the context of products liability law, and its relationship to "benefit of the bargain" under warranty law. App., 33a-34a. Agreeing with the California Supreme Court's decision in *Seely*, this Court in *East River* defined "economic" damage to mean damage to the product itself and business-related consequential damages proximately caused when a product fails to perform as the purchaser expected:

> [S]ince by definition no person or other property is damaged, the resulting loss is purely economic. Even when the harm to the product itself occurs through an abrupt, accident-like event, *the resulting loss due to repair costs, decreased value, and lost profits* is essentially the failure of the purchaser to receive the benefit of its bargain--traditionally the core concern of contract law. See E. Farnsworth, Contracts Sec. 12.8, pp. 839-840 (1982).

East River, 476 U.S. at 870 (emphasis added).

Because it failed to distinguish this Court's discussion of product liability law from its discussion of warranty law in *East River*, the Ninth Circuit misapprehended *East River*'s "benefit of the bargain" language as applying to damages caused by a defective product to other physically distinct property, regardless of whether the damaged property was manufactured, assembled and sold as a single finished product by the same seller. App., 34a-35a. "Economic loss" analysis focuses not on the damage to persons or property extrinsic to the product placed on the market by the manufacturer, but on unlimited expectation damages that could be proximately caused by a complex, defective product made up of several components that failed to perform the work expected. *East River*, 476 U.S. at 872-873. Allowing tort recovery against a Section 402A seller in situations where the complex product it sold damages only itself would, as *Seely* explained, swallow up the price/limitation-of-damages tradeoff allowed by warranty law. *East River* agreed with this assessment. *Id.*, 476 U.S. at 873 ("The manufacturer can restrict its liability, within limits, by disclaiming warranties or limiting remedies. See UCC Secs. 2-316, 2-719. In exchange, the purchaser pays less for the product.") The Court recognized the "need to keep products liability and contract law in separate spheres," *Id.*, 476 U.S. at 870-871, and accordingly performed its products liability analysis independent of its warranty law analysis:

> Products liability grew out of a public policy judgment that people need more protection from dangerous products than is

> afforded by the law of warranty. See *Seely v. White Motor Co.*, 63 Cal.2d 9, 15, 45 Cal. Rptr. 17, 21, 403 P.2d 145, 149 (1965). It is clear, however, that if this development were allowed to progress too far, contract law would drown in a sea of tort. See G. Gilmore, The Death of Contract 87-94 (1974). We must determine whether a commercial product injuring itself is the kind of harm against which public policy requires manufacturers to protect, *independent of any contractual obligation.*

East River, 476 U.S. at 866 (emphasis added).

Seely explained that warranty law could *not* shield a manufacturer from liability for defects in its product that create an "unreasonable risk of harm" to persons or property physically distinct from its product:

> The distinction that the law has drawn between tort recovery for physical injuries and warranty recovery for economic loss is not arbitrary and does not rest on the 'luck' of one plaintiff in having an accident causing physical injury. The distinction rests, rather, on an understanding of the nature of the responsibility a manufacturer must undertake in distributing his products. *He can appropriately be held liable for physical injuries caused by defects by requiring his goods to match a standard of safety defined in terms of conditions that create unreasonable risks of harm. He*

> *cannot be held for the level of performance of his products in the consumer's business unless he agrees that the product was designed to meet the consumer's demands.* A consumer should not be charged at the will of the manufacturer with bearing the risk of physical injury when he buys a product on the market. He can, however, be fairly charged with the risk that the product will not match his economic expectations unless the manufacturer agrees that it will.

Seely, 63 Cal. 2d at 18 (emphasis added). *East River* understood and agreed with the *Seely* analysis. *East River*, 476 U.S. at 871-872 .

The price/limitation-of-commercial damages balance that is the "benefit of the bargain" between the manufacturer and the original purchaser under warranty law has no application where, as here, the product placed into the stream of commerce by a manufacturer results in harm to persons or property physically distinct from the product sold by the manufacturer. Contrary to the Ninth Circuit's reading, nothing in *East River* is "inconsistent" with holding a product manufacturer fully liable in tort for damages caused by its product to persons and property physically distinct from the product. App., 35a.

D. The Ninth Circuit's Decision Places it in Direct Conflict with the Restatement Second and Other Circuits, Which Look to What the 402A Seller Delivered, Not to What a Downstream Consumer Sold, to Determine the "Product" Sold by the 402A Seller

Except for the Ninth Circuit (if the Ninth Circuit's revised decision stands), the unanimous rule is that if a defective product proximately causes damages to a person's property that is physically distinct from the defective product, the injured party is entitled to tort damages from the 402A seller of the defective product. That physically distinct property will be treated as "other property" for *East River* damage limitation purposes. This rule is logical and true even if both the defective product and the damaged property came to the injured owner by way of a transaction involving a non-402A seller as in this case and as in *Nicor*. Hence, as the Fifth Circuit held in *Nicor*, "the finished vessel delivered *by the manufacturer to the purchaser* is the product -- the object of the contract . . . ." *Nicor*, 876 F.2d at 505 (emphasis added).[9]

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[9] This determination is also made explicit in the Tentative Draft of the Restatement (Third) of Torts, which specifically defines and discusses "economic loss" to property, finding "other property" to be property "exclusive of the product itself":

> § 6. Definition of "Harm to Persons or Property": Economic Loss
>
> For purposes of this Restatement the term "harm to persons or property" includes economic loss only when caused by harm to:
>
> (a) the plaintiff's person;
>
> (b) the person of another when harm to the other interferes with a legally protected interest of the plaintiff;
>
> (c) *the plaintiff's property other than the defective product itself.*

Restatement (Third) of Torts: Products Liability, § 6 (Tentative Draft No. 2, March 13, 1995) (emphasis added).

The Third Restatement then defines "other property":

> *'Other property,' in its most basic sense, may be defined as tangible items belonging to the product purchaser, exclusive of the product itself.* Numerous cases hold that where damage is done by a defective product to any tangible item which is *physically distinct* from it, the damage to the 'other property' may be recoverable in tort.

Restatement (Third) of Torts: Products Liability, § 6, cmt d at 189 (Tentative Draft No. 2, March 13, 1995) (emphasis added).

No court other than the Ninth Circuit has ever held that a downstream sales contract between two consumers determines the boundaries of what a manufacturer's "product" is for purposes of defining "other property." Numerous cases, on the other hand, clearly focus on the product placed on the market by the manufacturer. In *Nicor*, the court looked to the "the object of the contract" between the shipbuilder and the plaintiff buyer to determine that equipment placed on the vessel by the plaintiff was "other property." *Nicor*, 876 F.2d at 505.

Likewise, in *Shipco*, 825 F.2d 925, the court denied recovery under *East River* against a manufacturer of a component part of a ship for economic damages caused by the part to the rest of the ship, where the component was sold by the shipbuilder to the first purchaser as original equipment; that is, it was part of the *complete ship* sold by the *manufacturer* to the first consumer/purchaser.[2/]

In *McDermott, Inc. v. Clyde Iron*, 979 F.2d 1068 (5th Cir. 1993), the court specifically stated how it determined the identity of "the product," and therefore,

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2/ In *Shipco* the court recognized that the question before it was, "what is the product?" *Id.*, 825 F.2d at 928. To answer this question, it asked,

> what is the object of the contract or bargain that governs the rights of the parties? The completed vessels were obviously the objects of the contract. Shipco (footnote omitted) did not bargain separately for individual components of each vessel. We are persuaded that those same vessels that were the object of the contract must be considered "the product" rather than the individual components that make up the vessels.

Id., 825 F.2d at 928. The point was that "Avondale (the manufacturer) sold the completed vessels to Shipco." *Id.*, 825 F.2d at 929. *Shipco*'s analysis was the equivalent of asking, "what did General Motors sell the consumer of a new Oldsmobile?" That case had absolutely nothing to do with the subsequent question, which the Ninth Circuit answered incorrectly, "if the first consumer sells the Oldsmobile to a second consumer a few years later, do the box of toys in the trunk, the child seat and the tool box the first owner sold with it become part of GM's "product" for product liability purposes?

"other property": "The object of the [purchaser]-[manufacturer] contract was the manufacture, design, and sale of the crane *and that is the relevant inquiry*." *McDermott*, 979 F.2d at 1077-1078 (emphasis added). *See also Mays Towing v. Universal Machinery Co.*, 755 F.Supp. 830 (S.D. IN. 1990) (damage to new engines placed in vessel were covered by warranty law; but damage to vessel caused by the defective engines was recoverable as "other property" under products liability law.)

It is undisputed that the skiff, net, fuel, spare parts, speed boats and miscellaneous equipment added to M/V SARATOGA by Madruga and sold to SARATOGA were *not* sold by Respondents at any time and are physically distinct individual products in their own right sold by other manufacturers after MARTINAC and MARCO sold the boat to Madruga. App., 6a. Under fundamental products liability law, because MARTINAC and MARCO did not place these items into the stream of commerce, these items cannot be considered Respondents' "product" for purposes of strict products liability. They are then, by definition, "other property" recoverable by SARATOGA.

E. The Ninth Circuit has Created Uncertainty in the Law

Where *East River* created order from chaos, the Ninth Circuit has created disorder in maritime law. Under *East River*, the spheres of products liability law and warranty law were clearly delineated. Under the Ninth Circuit's decision, however, a subsequent purchaser of a vessel is left to any warranty he may be able to obtain from the original purchaser. For all practical purposes, the

original purchaser, who did not manufacture the vessel, who is not a commercial seller or distributor, who did not place the vessel into the stream of commerce, and who cannot spread the risk of a product defect, would be loathe to assume the liability of the vessel manufacturer and offer to the second purchaser a warranty against unknown product defects.

> Products liability grew out of a public policy judgment that people need more protection from dangerous products than is afforded by the law of warranty. *See Seely v. White Motor Co.*, 63 Cal.2d 9, 15, 45 Cal. Rptr. 17, 21, 403 P.2d 145, 149 (1965).

East River, 476 U.S. at 866. Insofar as "other property" is concerned, however, the Ninth Circuit would take maritime products liability law back to the days of privity, leaving the second or subsequent end-user with no recourse for the destruction of "other property" by the defective product.

The Ninth Circuit's rule would base recovery on fortuity rather than principle. Hence, a first purchaser ("purchaser A") keeps a vessel for 20 years, adding many pieces of equipment to the ship during that period. So long as purchaser A owns the vessel the manufacturer can be held liable in tort for damage or destruction of this "other property" due to a defect in the ship. The manufacturer's liability would therefore increase every time the vessel is modified, so long as it is owned by the first purchaser. Yet if purchaser A sells the ship and all its additions to a second buyer ("purchaser B") after owning it for 20 years and one day, at the moment of sale the

manufacturer's liability for the "other property" *immediately* springs back to zero. As a result, the manufacturer's liability for precisely the same damage caused by precisely the same defect would turn on whether, by luck, the ship was sold the day before the defect manifested itself. *See* App., 41a, Noonan, J., concurring and dissenting.[8/]

Even more troublesome will be the suit in which a vessel manufacturer is sued for a personal injury caused by a defective piece of "other property" (e.g., a skiff) that the manufacturer did not sell with the vessel. The plaintiff would claim, under the Ninth Circuit's reasoning, that the defective "other property" became part of the vessel manufacturer's "product" when the vessel was sold to a second buyer and that the vessel manufacturer is therefore liable for damages caused to the plaintiff by this "other property."

Similarly, the manufacturer of a skiff that, because of a defective steering mechanism, turns and collides with the vessel from which it was launched, will claim that it cannot be held liable for damage to the ship because the skiff became part of the vessel manufacturer's "product" when the vessel, with the skiff, was sold to a second buyer.[2/] The defendant skiff manufacturer will therefore

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[8/] The district court also rejected this outcome as irrational. App., 176a.

[2/] This result would, of course, go far past *Shipco*, which decided only that the manufacturer of the steering mechanism that was part of the vessel when it was originally sold to the first purchaser by the manufacturer, could not be held liable for

contend that the "product" injured only itself. Moreover, because the skiff manufacturer did not provide the buyer with a warranty for such "economic damage," (which *East River* points out is customary) it cannot be held liable for any damage to the vessel. Similarly, because the vessel manufacturer did not provide a warranty for the skiff (after all, it was not even part of the vessel when it was sold), it too will have no liability for the damage.

F. The Law as it Existed Prior to the Ninth Circuit's Saratoga Decision Gave Certainty to Maritime Products Liability Law

No great calamities resulted from this Court's *East River* decision or the Fifth Circuit's decisions in *Shipco* and *Nicor*. *East River* provided a rational, principled basis for distinguishing between the realm of warranty law and products liability law, and for determining what the "product" at issue is for purposes of products liability claims. *Shipco* extended *East River* to establish that the complete vessel sold by the vessel manufacturer was the "product" for purposes of product defects in the component parts of the vessel. *Nicor* put both decisions into effect, holding that property added to the vessel purchased from the manufacturer was "other property" insofar as the vessel manufacturer was concerned. To determine "other property," all looked to what the

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damages that mechanism caused to other parts of the vessel. *Shipco*, 825 F.2d at 930-931. In the example above, under the Ninth Circuit's reasoning, the subsequently added equipment would become part of the manufacturer's "product," for which the manufacturer presumably could be sued. App., 34a-35a.

manufacturer sold to the first end-user purchaser.

East River created certainty and uniformity. The manufacturer could, under warranty law, limit its damages for economic consequences resulting from the destruction of the product itself as the result of a product defect. Consumers had the certainty of recourse to the manufacturer for damage to property other than the product itself where, as here, the product defect resulted in destruction of this "other property." The Ninth Circuit has destroyed this certainty, insulating manufacturers and leaving second and subsequent purchasers of a product with no effective recourse where a defect in the vessel results in destruction of "other property." The Ninth Circuit has erred, and its decision should be reversed.

VI. CONCLUSION

The Ninth Circuit's Final Opinion undermines and eviscerates fundamental tenets of products liability law. It places the Ninth Circuit in direct conflict with this Court's decision in *East River*, the decision of the Fifth Circuit in *Nicor*, and with Section 402A of the

Restatement (Second) of Torts. Only this Court now has the power to restore the uniformity and balance in maritime product liability law envisioned and required by *East River*. SARATOGA respectfully requests that this Court reverse the Ninth Circuit's decision as to "other property," and restore balance and uniformity in maritime products liability law.

Dated: November 29, 1996

Respectfully submitted,

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(5)

No. 95-1764

Supreme Court, U.S.
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In The

Supreme Court of the United States

October Term, 1996

SARATOGA FISHING CO.,

Petitioner,

vs.

J.M. MARTINAC & CO.;
MARCO SEATTLE, INC.,

Respondents.

On Writ Of Certiorari
To The United States Court Of Appeals
For The Ninth Circuit

RESPONDENTS' BRIEF

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QUESTIONS PRESENTED

1. Does a rule precluding tort recovery for loss of property acquired by a purchaser in a commercial sale transaction appropriately serve the goal of preserving the role of contract in maritime commerce?

2. Is the consequential loss of property produced by a product acquired in a commercial transaction, representing failure of the expected performance of the product, an economic loss for which tort recovery should be denied?

THE PARTIES

J. M. Martinac & Co. ("Martinac") is a privately held Washington corporation.

Marco Seattle, Inc. ("Marco") is a Washington corporation wholly owned by Marine Construction & Design Co., Inc., a privately held Washington corporation.

Saratoga Fishing Company, Inc. ("Saratoga"), was a privately held California corporation which has since formally dissolved, but retains the legal authority to litigate this matter under California Corporations Code § 2010.

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I. OPINIONS BELOW

The opinion of the Ninth Circuit Court of Appeals in this matter was filed on October 26, 1996, (Appx. 4a-41a)[1] and is reported at 69 F.3d 1432 (9th Cir. 1995). Neither the District Court's Findings on Liability (Appx. 114a-172a), nor its Findings on Damages (Appx. 173a-185a) are reported. Both the original opinion of the Ninth Circuit Court of Appeals filed April 25, 1995 (Appx. 43a-78a), and the modified opinion filed August 4, 1996 (Appx. 79a-113a) were withdrawn from publication by the Ninth Circuit.

II. JURISDICTION

The Ninth Circuit Court of Appeals entered its order denying the motion for rehearing made by the Petitioner, Saratoga Fishing Company ("Saratoga"), on January 30, 1996. (Appx. 1a) Saratoga filed its Petition for Writ of Certiorari on April 29, 1996. This Court granted certiorari on October 15, 1996. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1). The jurisdiction of the District Court was predicated upon the admiralty jurisdiction of the federal courts under 28 U.S.C. § 1333.

III. STATEMENT OF THE CASE

This case arises from the sinking of the M/V Saratoga, a 191 foot steel-hull tuna-seining vessel. The M/V

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[1] References to the appendix, or "Appx." are to Petitioner's Petition for Writ of Certiorari. The Court previously entered an order permitting Petitioner to dispense with preparation of a separate appendix.

Saratoga was in service for fourteen years before she suffered a catastrophic hydraulic failure, burned and sank. The fire started when a major hydraulic supply hose, previously known by the captain and chief engineer to be leaking, burst during fishing operations. The hose was a replacement hose of unknown quality, specification and installation.

This action proceeded to trial on a product liability theory. The District Court found that this loss was caused in major part by poor maintenance, extensive modifications to the hydraulics system, and the careless actions of the Captain and Chief Engineer which the court found "borders on irresponsible conduct." (FL 143, 155, 167, Appx. 164a, 168a, 171a.)[2] Nevertheless, the Respondents were held 1/3 at fault for the loss.

The M/V Saratoga was a "fishing machine" comprised of the thousands of components necessary to locate, harvest, store, transport and deliver a "catch" of tuna. To accomplish this mission, a tuna seiner *must* carry and utilize a purse seine net, a skiff and other fishing equipment necessary to capture and bring the tuna aboard, where it is frozen in super-cooled brine during the journey to market. If any of the critical components of this "fishing machine" fails to perform, the vessel owner is either unable to catch tuna, unable to effectively store the catch, or unable to transport the catch to market; and is thereby unable to sell raw tuna for a profit.

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[2] For the convenience of the Court references include the numbers of the Trial Court's "Findings on Liability" ("FL") or "Findings on Damages" ("FD"), as well as to the Petitioner's Appendix ("Appx.").

The purse seine tuna fishing method was developed during the late 1950's and early 1960's. Previously, tuna fishing involved the use of small, wooden-hull "bait boats," so-called because the tuna were caught using fishing poles and bait. In the late 1950's, a few tuna fishing vessel owners began pioneering the use of the "purse seine" method of harvesting tuna, whereby a purse seine net is dropped into the water, with one end attached to a skiff.[3] The skiff then remains stationary while the tuna seiner comes about, deploying the rest of the net to encircle a school of tuna. The tuna seiner circles back to the skiff, where the two ends of the net are joined, and the bottom of the net is closed, thereby trapping the tuna. (FL 2, Appx. 118a; Testimony, Trial Transcript Vol. X, pp. 49-54)

At first, bait boat owners took their wooden bait boats to small shipyards to be refitted to carry a skiff, a net, and the hydraulic winch, boom, and other equipment necessary to deploy and retrieve the net. Because the vessel owners, and not the shipyards, developed this new fishing method, the vessel owners largely directed the retrofitting procedures. Inevitably, as the related equipment became bigger, heavier, and more powerful, the wooden bait boats proved to be too small a platform, and larger steel-hull vessels were needed to carry the new equipment, and the record harvests being netted. These

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[3] A skiff is a motor craft which, when not in use, rides "piggyback" on the stern ramp of the mother ship. The skiff serves the dual purposes of holding one end of the net while the net is deployed by the mother ship around a fish school, and as the mother ship's life boat.

vessel owners were the driving force behind the evolution to a completely new class of fishing vessel specially designed for the needs of modern tuna seining, capable of traveling great distances, carrying heavy power equipment, and properly processing and storing the resulting catch so that the tuna would be fit for human consumption at the end of a long voyage. (Testimony, Trial Transcript Vol. X, pp. 49-54)

A handful of small shipyards, including J.M. Martinac & Co. ("Martinac"), began custom building steel hull tuna seiners to order for vessel owners in the 1960's. (Testimony, Trial Transcript Vol. X, pp. 52-53) By 1971, when the M/V Saratoga was built, the construction of each Martinac tuna seiner was still a product of detailed collaboration between shipowner and shipyard, with the shipowner selecting and approving the selection of various components and their physical arrangement aboard a vessel.[4] (Testimony, Trial Transcript Vol. X, pp. 55-60)

Joseph Madruga ("Madruga") was one of the pioneers of modern tuna-seining, first using converted bait boats, and then commissioning construction of the new steel hull seiners. (FL 1, Appx. 118a.) Saratoga's contention notwithstanding (Petitioner's Brief, p. 14), Madruga was decidedly *not* an unsophisticated consumer

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[4] The statement by Saratoga that " Martinac and Marco sold the boat to Madruga is not accurate. Madruga contracted with Martinac for construction of the vessel (*Trial Ex. A*, Trial Transcript Vol. X, pp. 72, 74). Certain Marco brand hydraulic machinery was specified for inclusion on the vessel (*Trial Ex. B*, Trial Transcript Vol. X, pp. 72, 74). Marco was a vendor to Martinac, but was not a party to the sale of the vessel by Martinac to Madruga.

lacking the economic power to bargain for product specifications or allocation of risk through warranty. The M/V Saratoga was the third of *seven* steel hull tuna seiners which Madruga commissioned from Martinac, the purchase price of the M/V Saratoga being $2,200,000. (Testimony, Trial Transcript Vol. X, pp. 70:10-20; Trial Ex. A, Trial Transcript Vol. X, pp. 72, 74) Madruga negotiated with Martinac over the specifications and equipment for the M/V Saratoga. (Testimony, Trial Transcript Vol. X, pp. 72-73:12-16) Additionally, both Madruga and an engineer he employed to supervise construction were at the shipyard during construction of the M/V Saratoga and ordered numerous changes to the vessel during the course of construction. (Testimony, Trial Transcript Vol. X, pp. 81:17-25, 84-87)

The contract between Madruga and Martinac provided a six-month limited warranty that the vessel and her components were of merchantable quality and properly installed. All other warranties were expressly disclaimed. (Trial Ex. A, Trial Transcript Vol. X, pp. 72, 74.)

As delivered by Martinac, in accordance with the contract, the M/V Saratoga was *not* complete or able to operate as a tuna seiner. Madruga bargained for the M/V Saratoga to be delivered as an incomplete fishing vessel requiring the separate purchase of a net, skiff, speedboats[5] and other miscellaneous equipment including

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[5] At this time tuna seiners operating in the eastern tropical Pacific carried a number of small speedboats to "round up" porpoise, much like cowboys round up cattle. Once the porpoise (and the tuna, which follow the porpoise) are rounded up, the tuna seiner encircles the porpoise and tuna with the seine net.

navigational and communications electronics. (FL 9, Appx. 121a; FD 2, Appx. 175a-176a.) The District Court found the value of these items at the time of loss to be $484,905. (FD 17, Appx. 184a.) Only after Madruga completed assembly of the M/V Saratoga as a "fishing machine" by adding these items was she able to put to sea to accomplish the mission for which Martinac had begun the assembly of her components. (FL 9, Appx. 121a.)

In March, 1974, Saratoga purchased the completed, fully outfitted M/V Saratoga from Madruga's corporation for $2,950,000 thereby earning Madruga's corporation a substantial profit. (Trial Ex. Z, Trial Transcript Vol. VII, pp. 13, 19) The transaction between Saratoga and Madruga thus represents the *first* time that the M/V Saratoga was sold as a completed fishing vessel capable of performing its mission. Saratoga bought the M/V Saratoga as a complete, integrated unit including all of the items which Saratoga claims are "other property," except for the ship's lost tuna catch. (FL 11, 12, Appx. 121a, 122a.) There is no dispute that sale of the M/V Saratoga from Madruga's corporation to Saratoga was a business transaction between commercial entities; and that the object of Saratoga's bargain was a fully integrated, operational tuna seiner, including everything necessary to conduct fishing operations. Saratoga bought the vessel "as is, where is," with no warranty other than that "said vessel and her appurtenances will be in operable condition upon delivery of the Bill of Sale." (Trial Ex. Z, Trial Transcript Vol. VII, pp. 13, 19) Presumably, the disclaimer of warranties on the vessel and all of her appurtenances was in exchange for a lower purchase price than would

have been charged if Madruga had included extensive warranties.

The M/V Saratoga burned and sank on January 16-17, 1986,[6] along with all of the property acquired by Saratoga from Madruga, except for the skiff, which was deliberately scuttled after the crew of the M/V Saratoga were rescued.[7] Saratoga also lost the expected performance of the vessel – the catch of tuna aboard. Because the vessel sank before it was able to deliver the catch in proper condition to the cannery for sale, Saratoga lost the profit it expected to receive when it originally purchased the vessel.

IV. SUMMARY OF ARGUMENT

By looking to the object of Saratoga's bargain and denying tort recovery for direct loss of the physical property acquired as part of Saratoga's bargain, the Ninth Circuit properly applied the economic loss rule adopted in *East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858 (1986). Adoption of the economic loss rule in *East River* represents a policy-based preference for rules

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[6] Contrary to Saratoga's assertion, it is not true that "The crew just managed to get off the ship into the skiff before the vessel sank." (Petitioner's Brief at pp. 2-3) Rather, the crew abandoned the vessel 10-20 minutes after the fire began, and were picked up approximately three hours later by another vessel. The M/V Saratoga finally sank the next morning, approximately 14 hours after the fire began. (FL 16, 17, 79, Appx. 123a, 142a.)

[7] The skiff aboard at the time of loss was a replacement for the skiff acquired with the vessel in 1974.

of contract and risk allocation methods, including insurance, which have long acceptance in maritime commerce. To permit tort recovery for failed contractual expectations in a commercial setting would be to extend tort recovery beyond its intended purpose, which is to afford a remedy to injured consumers, without the ability to negotiate product specifications or risk of loss, forced to rely on manufacturers for product needs. In product liability parlance, application of tort principles in commercial cases where these policies are not furthered, is "misuse."

The economic loss rule represents a contract approach which sets the boundary on tort recovery in commercial cases by excluding direct loss of the physical object of a purchaser's bargain, and indirect consequential losses, because the risk of commercial loss is understood to have been the subject of the parties' negotiation and bargain. These losses must be recovered, if at all, under contract law. This contract approach protects and enforces the contractual risk allocations of the commercial parties, as well as all other parties in the commercial chain of manufacture, distribution and sale, thereby preserving uniformity and predictability in maritime commerce.

The tort approach advanced by Petitioner would respect the parties' contractual risk allocation only to the extent of the "product" first sold to a "user." Any components added or associated thereafter would be "other property" recoverable in tort, even when these additional components are a major part of the plaintiff's bargain. Since Petitioner's tort approach does not focus on the plaintiff's bargain, its application will necessarily nullify voluntary risk allocation methods long employed

in maritime commerce. In turn, commercial actors will find difficulty structuring their business behavior and will additionally find themselves exposed to indeterminate tort liability. In an effort to reign-in such tort liability, courts applying maritime law will be forced to engage in the difficult line-drawing which the Court sought to avoid in *East River*.

The economic loss rule simply means that in commercial settings, where it is presumed that all parties have the ability and motivation to bargain for risk allocation, "a bargain is a bargain." Since commercial parties can negotiate their rights and remedies, any remedy for loss-of-bargain must itself be bargained for. Otherwise, judicial assistance to the party who failed to bargain for its own protection, will result in disruption of the voluntary risk allocation achieved by the parties. While the Ninth Circuit correctly looked to the object of Petitioner's commercial bargain to determine the economic loss, it stopped short in its analysis by failing to consider that Petitioner's lost tuna catch, a direct result of the failure of Petitioner's commercial purchase to perform as expected, also represented "insufficient product value." Two Fifth Circuit maritime cases and numerous state court decisions applying the economic loss rule would deny tort recovery for the lost fish catch as a failed contract expectancy. In order to give effect to the policy choices underlying the economic loss rule, and in the interests of predictability and uniformity in maritime law, the decision awarding tort damages for loss of the tuna catch must be reversed.

V. ARGUMENT

A. The remedy for loss of the benefit of a commercial maritime bargain lies only in contract.

This case involves application of the economic loss rule adopted by this Court in *East River, supra,* 476 U.S. 858, which states the proposition that loss of a commercial bargain occasioned by product failure is not compensable in tort. This includes loss of the product itself and consequential economic losses for which contract law provide a recovery. The disappointed commercial purchaser's remedy arises from the consensual nature of the commercial relationship, and has its genesis in the purchaser's bargain. "The character of a loss determines the appropriate remedies, and, to determine the character of the loss, one must look to the product purchased by the plaintiff, not the product sold by the defendants." *Pulte Home Corp. v. Osmose Wood Preserving, Inc.*, 60 F.3d 734, 741 (11th Cir. 1995), *citing King v. Hilton-Davis,* 855 F.2d 1047 (3rd Cir. 1988), *cert. denied,* 488 U.S. 1030 (1989). Thus, if the failed "product" was acquired in a commercial relationship, an upstream seller has no tort liability for: (a) loss of the object of the commercial purchaser's bargain (often termed "the product"), or for (b) consequential economic losses susceptible of contract recovery.

The economic loss rule serves to protect the marine industry's expectation that voluntarily risk allocations will be honored. In *East River* this Court recognized that "the main currents of tort law run in different directions from those of contract and warranty . . . " (476 U.S. at 873, n.8) and that "if this development *[of products liability in a commercial context]* were allowed to progress too far, contract law would drown in a sea of tort." 476 U.S. at 867. The economic loss rule recognizes the "need to keep products liability and contract law in separate spheres and to maintain a realistic limitation on damages." 476 U.S. at 871. *East River* affirmed that contract law is supreme in commercial intercourse, and that tort does not provide an optional legal regime for the disappointed commercial purchaser who could have bargained for a contractual remedy for the loss suffered.

Within maritime commerce, the challenge to the body of contract law presented by ever-expanding tort liability is so great, and the need for appropriate, predictable limitations on damages so compelling, that this Court did not limit application of the economic loss rule to situations where the purchaser *actually has* a contract remedy that would be displaced by a tort remedy. Although the disappointed charterers in *East River* were without a contract remedy (like Saratoga, they specifically took the ship "as is"), the Court saw "no reason to extricate the parties from their bargain." 476 U.S. at 875. With elegant simplicity *East River* teaches: "a bargain is a bargain!"

While Saratoga's Brief pays lip service to the "clear delineation" of the separate spheres of contract and tort, Saratoga fails to recognize that implementation of the economic loss rule requires identifying the disappointed commercial purchaser's bargain, and then limiting the purchaser to bargained-for remedies for expectancy losses. This "pure" contract approach follows from the proposition that contract and warranty rules are better suited than tort for the resolution of commercial controversies involving failed contractual expectations. As this

Court remarked: "[W]arranty law sufficiently protects the purchaser by allowing it to obtain the benefit of its bargain." 476 U.S. at 873.

Drawing only upon tort principles, Saratoga proposes to define "the product" as either (a) what was originally sold to the first user of the product; or (b) what the last "402A Seller" in the chain of distribution sold. Saratoga's Brief is not clear as to which particular definition it favors and offers no discussion as to the reasons that might support one approach over the other. Similarly, the *amicus* brief of All Alaskan Seafoods provides no guidance or rationale. Both Saratoga and All Alaskan Seafoods seem to be asking this Court to retreat from *East River* and allow tort concepts to control application of contract principles, all under the guise of implementing the economic loss rule applied by *East River*. As discussed *infra*, the result will be greater confusion in the law and blurring of the distinction between tort and contract.

Saratoga's approach is to artificially apply a tort-based definition of the "product" to implement a rule which is intended to exclude tort recovery for loss-of-bargain. The result is an arbitrary "product" / "other property" distinction which has no relationship to the purchaser's bargain, or to the public policy goal of preserving voluntary contractual risk allocations. In practice, this means that a *portion* of a commercial purchaser's bargain becomes compensable in tort (*i.e.*, the loss of that portion of the bargain which was *not* part of the first sale by a manufacturer or last sale by a "402A Seller"), while the loss of the rest of the purchaser's bargain (*i.e.*, whatever was neither encompassed by the original sale by a

manufacturer, nor the last sale by a "402A Seller") would *not* be compensable in tort. Saratoga's approach is incongruous if not irreconcilable with *East River*.

If only contractual remedies are permitted for loss of a commercial purchaser's bargain, there is no principled basis for artificially differentiating one segment of the purchaser's bargain from another with the application of tort concepts. The *only* basis for extending tort remedy into the realm of commercial contract should be some overriding public policy.[8] But where only loss of the benefit of a commercial bargain is involved, "the reasons for imposing a tort duty are weak and those for leaving the party to its contractual remedies are strong." 476 U.S. at 871. Moreover, as to those elements of a plaintiff's bargain which are arbitrarily deemed appropriate for tort recovery under the test suggested by Saratoga, the same problem exists that was identified in *East River*: tort law provides no realistic limitation on damages, making it difficult for manufacturers to structure their business behavior. 476 U.S. at 871, 874.

Saratoga complains that an economic loss rule which employs an "object of the bargain" analysis improperly determines a manufacturer's liability based on fortuity, *i.e.*, whether the manufacturer is "lucky enough" to have its product incorporated into another's product and then resold. The line between tort and warranty recovery for

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[8] The prime example being the tort remedy provided to the individual user or bystander injured as a result of the failure of a defective commercial product, who would have had no opportunity to secure warranty protection.

economic loss is *not* arbitrarily based on fortuity.[9] Saratoga's reasoning is fallacious, because liability (or lack thereof) under the economic loss doctrine does not hinge on the fortuity of prior sales, but rather, from the parties' conscious commercial choice, as evidenced by their contract.[10]

Ironically, Saratoga's *own* proposed rule would condition the availability of tort recovery to a commercial plaintiff on the fortuity of having property added to the product at some time subsequent to either the first sale to a user or the last sale by a "402A Seller," even though such other property was part of such plaintiff's bargain. Worse yet, a supplier of a single component would be liable under *Saratoga's* proposed regime for the loss of an entire vessel. Such liability would be predicated on the *misfortune* of having its component added to a vessel *after* the initial sale to a user, when such component could just

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[9] "The distinction that the law has drawn between tort recovery for physical injuries and warranty recovery for economic loss is not arbitrary and does not rest on the 'luck' of one plaintiff in having an accident causing physical injury." *476 U.S.* at 871, *citing Seely v. White Motor Co.*, 63 Cal.2d 9, 18 (1965). In this brief we use "contract" to include the modern commercial law of warranty, and to distinguish the basis for liability from claims founded purely in "tort" – the former arising from a consensual commercial relationship, and the latter from some misadventure bringing plaintiff and defendant together.

[10] In effect, Saratoga and its *amicus* are suggesting that a creative plaintiff is to be given a financial remedy by the judiciary "for free" which that same plaintiff declined to "buy" in the commercial transaction by which it acquired the product which failed.

as well have been "original equipment." Under Saratoga's proposed regime, the rest of the vessel is "other property" vis-a-vis the subsequently added component, even though the purchaser acquired the integrated package, including the new component, as part of the same commercial bargain. There is no valid reason to permit the tort invasion of commercial contract law presented by this novel and arbitrary approach, which is wholly unpredictable from the commercial seller's perspective.

B. The economic loss rule strikes a balance between the policies underlying product liability law and the traditional maritime law goals of uniformity and predictability.

"Products liability grew out of a public policy judgment that people need more protection from dangerous products than is afforded by the law of warranty." *476 U.S.* at 866, *citing Seely v. White Motor Co.*, 63 Cal.2d 9, 15 (1965). The reasons courts found warranty law afforded insufficient protection to consumers were: (1) consumers of off-the-shelf products generally lack the sophistication and economic power to effectively bargain as to the specifications of the product, or the risk of loss relating to use of a product, and are forced to rely on manufacturers to provide for their needs;[11] (2) the ability of consumers to effectively insure against product-related losses is uncertain, while manufacturers of mass-produced goods can readily insure against such losses, spreading the cost of

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[11] *See*, Restatement (Second) Torts § 402A, comment *c*.

such protection through slight product price increases;[12] and, (3) judicial displeasure with the lack of privity defense which defeated personal injury claims by consumers, end-users, bystanders, and others similarly situated.[13]

These reasons – developed in the consumer-mass-produced-goods context – have no application in commercial transactions, particularly transactions involving the construction and sale of commercial marine vessels. Specifications for commercial marine vessels are typically the subject of a negotiated contract between a shipyard and a sophisticated commercial purchaser.[14] Commercial maritime purchasers are not forced to rely on the manufacturer to fill their needs, and generally, as in this case, have the knowledge and the bargaining power to effectively negotiate the risk of loss. Commercial buyers are capable of gauging the risk and deciding whether to negotiate a product warranty or procure insurance.[15]

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[12] *Greenman v. Yuba Power Products, Inc.*, 59 Cal.2d 57, 63 (1963).

[13] *MacPherson v. Buick Motor Co.*, 217 N.Y. 382, 111 N.E. 1050 (1916). The *MacPherson* rule was tacitly recognized in an admiralty action in *Seas Shipping Co. v. Sieracki*, 328 U.S. 85 (1946).

[14] In the present case, while the negotiated contract was a mere 5 pages (Trial Ex. "A" Trial Transcript, Vol. X, pp. 72, 74), the basic specifications for the vessel negotiated between Martinac and Madruga are 108 pages in length. (Trial Ex. "B" Trial Transcript, Vol. X, pp. 72, 74.)

[15] The lack of essential purpose for applying product liability to commercial transactions has led some courts to develop rules excluding tort liability completely in certain commercial situations. In *Kaiser Steel Corp. v. Westinghouse Electric Corp.*, 55 Cal.App.3d 737, 748 (1976), the California

Commercial maritime concerns are almost universally insured. Indeed, Saratoga was insured for the very losses which are the subject of the underlying action. Maritime commerce decidedly does *not* involve the uncertainty as to the user's ability to procure insurance that motivated the creation of strict product liability to protect those acquiring goods for personal use or those suffering personal injuries from defective goods. The availability of insurance to commercial parties was a factor underlying the Court's decision not to disturb the charterers' bargain in *East River*, 476 U.S. at 871.

The commercial product-user has the ability to spread the cost of procuring such insurance through price adjustments for its own good or services. In many instances, the commercial purchaser's ability to spread the cost of insurance through the pricing of its own goods or services to the public may be superior to that of the seller of a commercial product. For example, commercial shipbuilders like Martinac do not produce sufficient numbers of vessels to permit efficient cost-spreading by

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Appellate Court held that product liability does not apply where commercial parties have bargained at arms' length, from positions of relatively equal bargaining power, over specifications and risk of loss, reasoning that in these commercial situations, "any societal interest in loss shifting is absent." A few states have reached the same end result by holding the Uniform Commerrcial Code preempts product liability in the commercial context. *See* cases collected in Annot., *Pre-emption of strict liability in tort by provisions of UCC Article 2*, 15 ALR4th 971. *See also*, H.W. Titus, *Restatement (Second) of Torts Section 402A and the Uniform Commercial Code*, 22 Stanford L. R. 713 (1970) for a historical discussion of the tension between § 402A and the UCC.

price increases which would not affect their competitiveness. Conversely, the cost of procuring insurance is a cost of doing business to commercial tuna fishermen, which is eventually and readily passed through to the millions of consumers of canned tuna in the form of minuscule price increases. The commercial user also often has far superior knowledge of the actual risks which the product will encounter and is in a far better position to quantify the risks and potential losses. For example, a substantial portion of the trial testimony in this case related to product misuse, inadequate vessel maintenance, major modifications to the vessel's hydraulic system, intentional disabling of safety devices, and so on,[16] all of this was initiated and controlled by Saratoga, but unknown to Martinac and Marco. It is also apparent that insurance is a far better – and ultimately fairer – method of risk transfer. Not only is the risk known to (or reasonably discoverable by) the insurer, it is quantified by insurance contract. In the present case, the insurance company required annual vessel inspections and dictated trading limits, periodic dry-docking, manning requirements, and otherwise acted to minimize the risk for which it accepted premium payments.[17] None of these options was available to Martinac or Marco.

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[16] *See generally,* FL 50-69, 131-143, 154-156, Appx. 133a-139a, 160a-164a, 167a-168a.

[17] *See* numerous annual insurance survey reports admitted as Trial Exs. 217, 220-233, 235-256, at Trial Transcript Vol. V, p. 106; *See also,* Tuna Boat Survey Requirements, Trial Ex. 215, Trial Transcript Vol. VI, p. 179, Vol. VII, p. 122.

Finally, the problem of lack of privity depriving a commercial product user of the ability to procure warranty protection is non-existent. Every commercial purchaser has a full range of contract options and an extensive body of commercial law exists for resolving controversies involving loss-of-bargain. Accordingly, an uncompensated commercial loss is the product of a rational economic choice by a commercial purchaser dealing at arms' length, rather than a result of non-options unilaterally imposed upon a powerless unsophisticated consumer.

Uniformity and predictability are core concerns of maritime law. *See, e.g., The Lottawanna,* 88 U.S. 556, 575 (1875). These concepts are promoted by allowing commercial parties the freedom to encounter the risks of the marketplace as they see fit based on rational economic decisions, and evidenced by their contracts and industry practices. Warranty and insurance afford commercial parties satisfactory means of obtaining redress for damage from a product failure. In maritime commerce, when only expectancy damages are sustained, there simply is no remedial gap to be filled by tort.

As a body of commercial law, maritime law should embrace and support the lawful practices of the commercial interests it serves, recognizing the realities of bargaining over risk of loss and insuring against commercial risks. This Court should reject the proposed rule which would endorse the *ex post facto* tort transfer of losses

sought in the name of Saratoga by its insurer who contractually bound itself to accept the precise risk encountered.[18]

The warranty provision of the typical vessel construction contract reflects an allocation of specified post-delivery risks as an integral part of the pricing process. This philosophy is found in other situations within the maritime context. *See, e.g., Carnival Cruise Lines v. Shute,* 499 U.S. 585, 592 (1991) (*the financial effect of forum selection and choice of law clauses likely will be reflected in the value of the contract as a whole*); *Roby v. Corporation of Lloyd's,* 996 F.2d 1353, 1363 (2d Cir. 1993). Such clauses reflect agreement as to which party will bear the cost of insurance, and for what period of time, *i.e.,* whether the ultimate risk of vessel loss shifts to the vessel owner's insurer from the shipbuilder's insurer.[19]

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[18] Respondents are not arguing for abrogation of subrogation, but simply that under the commercial circumstances of this case, there is no *bona fide* claim for the insurer to pursue.

[19] Several common law courts have explicitly approved contractual risk shifting between commercial parties. For example, allocation of the burden of purchasing insurance, as a *de facto* shifting of risk by contract, was discussed and succinctly upheld *in Delta Air Lines, Inc. v. Douglas Aircraft Company,* 238 Cal. App. 2d 95, 104-05 (1965): "In short, all that is herein involved is the question of which of two equal bargainers should bear the risk of economic loss if the product sold proved to be defective. Under the contract before us, Delta (or its insurance carrier, if any) bears that risk in return for a purchase price acceptable to it; had the clause been removed, the risk would have fallen on Douglas (or its insurance carrier, if any), but in return for an increased price deemed adequate by it to compensate for the risk assumed. We can see no reason why

While warranty and insurance provide commercial parties the predictable risk allocation solution needed to enable them "easily to structure their business behavior" (476 U.S. at 870), the tort-based approach advocated by Saratoga yields unpredictable hindsight-driven results and indeterminate damages. As this Court recognized in *East River,* 476 U.S. at 872-874:

> Contract law, and the law of warranty in particular, is well suited to commercial controversies of the sort involved in this case because the parties may set the terms of their own agreements. . . . A warranty action also has a built – in limitation on liability, whereas a tort action could subject the manufacturer to damages of an indefinite amount. The limitation in a contract action comes from the agreement of the parties and the requirement that consequential damages, such as lost profits, be a foreseeable result of the breach. . . . In products-liability law, where there is a duty to the public generally, foreseeability is an inadequate brake. (*Citations omitted*).

The *East River* approach emphasizing the supremacy of contract law over tort law in commercial application is in complete harmony with the policies underlying strict product liability, the public policy supporting freedom of

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Delta, having determined, as a matter of business judgment, that the price fixed justified assuming the risk of loss, should now be allowed to shift the risk so assumed to Douglas, which had neither agreed to assume it nor been compensated for such assumption." [*footnotes omitted*], cited with approval in *Delta Airlines, Inc. v. McDonnell Douglas Corp.,* 503 F.2d 239 (5th Cir. 1974), *cert. denied,* 421 U.S. 965 (1975) [*upholding exculpatory clause as to expense of repairing collapsed nosegear*].

contract in commercial relations, and the reality of insurance in maritime commerce. Since the policies underlying strict product liability are not served by its application in the commercial realm, the parties are best left to their contracted-for remedies, if any, or risk transfer through insurance.

C. Saratoga seeks to emasculate *East River's* widely-accepted economic loss rule, which looks to the object of the commercial plaintiff's bargain to define the exclusive sphere of contract.

East River is based on the premise that products liability law must not be allowed to distort the contractual arrangements the commercial parties have negotiated. To avoid overriding commercial parties' voluntary risk allocation as expressed in their contract, the Court necessarily focused on the charterers' bargain and refused to allow tort recovery for their loss of that bargain, even though the charterers had no warranty remedy available. 476 U.S. at 875.

The preference stated in *East River* for contractual over tort remedies in commercial disputes involving failed contract expectations has been unanimously accepted by federal courts sitting in admiralty,[20] state

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[20] *Shipco 2295, Inc. v. Avondale Shipyards, Inc.*, 825 F.2d 925, *cert. denied*, 485 U.S. 1007 (1987); *Nicor Supply Ships Associates v. General Motors*, 876 F.2d 501 (5th Cir. 1989); *McConnell v. Caterpillar Tractor Co.*, 646 F.Supp. 1520 (D. N.J. 1986); *Petroleum Helicopters, Inc. v. Avco Corp.*, 930 F.2d 389, 391-393 (5th Cir. 1991); *McDermott, Inc. v. Clyde Iron*, 979 F.2d 1068, 1078 (5th Cir. 1992), *rev'd on other grounds*, 511 U.S. 202 (1994); *Exxon Shipping Company v. Pacific Resources, Inc.*, 835 F.Supp. 1195, 1201-1202 (D. Hawaii 1993); *Saratoga Fishing Co. v. Marco Seattle, Inc.*, 69 F.3d 1432 (9th Cir. 1995); *Karshan v. Mattituck Inlet Marina & Shipyard, Inc.*, 785 F.Supp. 363, 364 (E.D.N.Y. 1992)

courts applying maritime law,[21] and widely embraced by both federal and state courts applying state product liability law.[22]

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[21] *Stanton v. Bayliner Marine Corp.*, 123 Wash.2d 64 (1993), *cert. denied*, ___ U.S. ___, 115 S.Ct. 78 (1994); *Lewinter v. Genmar, Inc.*, 26 Cal.App.4th 1214 (1994).

[22] Ironically, while the Court in *East River* recognized incorporation into the general maritime law of the common law product liability principles, the common law has, in the wake of *East River*, reciprocated. An overwhelming number of courts and jurisdictions have adopted the holding and reasoning of *East River* to state products liability law. *See, e.g., International Ore & Fertilizer Corp. v. SGS Control Services, Inc.*, 38 F.3d 1279, 1283-1284 (2d Cir. 1994), *cert. denied*, 115 S. Ct. 2276 (1995) (New York law); *Rocky Mountain Helicopters, Inc. v. Bell Helicopter Textron, Inc.*, 24 F.3d 125, 129-130 (10th Cir. 1994) (Texas law); *Hininger v. Case Corp.*, 23 F.3d 124, 125-127 (5th Cir. 1994) (Texas, Illinois, and Idaho law all follow economic loss rule); *Miller's Bottled Gas, Inc. v. Borg-Warner Corp.*, 955 F.2d 1043, 1050 (6th Cir. 1992) (Kentucky law); *Miller v. U.S. Steel Corp.*, 902 F.2d 573, 574-575 (7th Cir. 1990) (Wisconsin law); *Aloe Coal Co. v. Clark Equip. Co.*, 816 F.2d 110 (3d Cir. 1987), *cert. denied*, 484 U.S. 853 (1987) (Pennsylvania law); *2000 Watermark Ass'n., Inc. v. Celotex*, 784 F.2d 1183, 1185-1187 (4th Cir. 1985) (South Carolina law); *Bocre Leasing Corp. v. General Motors Corp.*, 840 F. Supp. 231, 234 (E.D.N.Y. 1994), *questions certified*, 20 F.3d 66 (2d Cir. 1994), *certified questions answered*, 645 N.E.2d 1195 (N.Y. 1995) (New York law); *Canal Elec. Co. v. Westinghouse Elec. Corp.*, 756 F. Supp. 620, 629-630 (D. Mass. 1990) (Massachusetts law); *PPG Indus. Inc. v. Sundstrand Corp.*, 681 F. Supp. 287, 291 (W.D. Pa. 1988) (declining to choose which state law applies, since California, Illinois, North Carolina and Pennsylvania would all follow

The Fifth Circuit in *Shipco 2295, Inc. v. Avondale Shipyards, Inc.*, 825 F.2d 925, *cert. denied*, 485 U.S. 1007 (1987) applied an "object of the bargain" test, emphasizing that a purchaser bargains for a finished product, not for the various components that comprise the product:

> In attempting to identify the product, our analysis leads us to ask what is the object of the contract or bargain that governs the right of the parties? The completed vessels were obviously the objects of the contract. [*Plaintiff*] Shipco did not bargain separately for the individual components of each vessel. We are persuaded that those same vessels that were the object of the contract must be considered "the product" rather than the individual components that make up the vessels. 825 F.2d at 928 (*footnote omitted*).

Saratoga attempts to distinguish *Shipco* by likening the Madruga-Saratoga sale transaction to a sale between consumers of a used Oldsmobile with toys, a child seat, and a tool box in the trunk. (Petitioner's Brief, p. 30 n. 7.) The comparison is not apt. The relevant transaction in this case was commercial, and *East River* spoke directly to the absence of tort recovery for loss of a commercial bargain. *Shipco* merely restated that the best way to apply the economic loss rule is to look at the object of the parties' bargain. In the present case, the equipment added to the M/V Saratoga was both critical to the ability of the

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economic loss rule set forth in *East River*); *Richard O'Brien Cos. v. Challenge-Cook Bros., Inc.*, 672 F. Supp. 466, 471-473 (D. Colo. 1987) (Colorado law); *Utah Int'l., Inc. v. Caterpillar Tractor Co.*, 108 N.M. 539, 541-542, (Ct. App.), *cert. denied*, 108 N.M. 354 (1989) (New Mexico law).

vessel to fulfill its mission, and an integral part of Saratoga's bargain.

Saratoga has cited a number of cases involving asbestos contamination, arguing that they reject the "object of the bargain" approach. These cases do not support abandonment of the bargain-based approach in commercial maritime cases. The asbestos cases involve application of state law, not maritime law, and they take an approach similar to the "intermediate" approach to products liability which was specifically rejected in *East River*, 476 U.S. at 869-870. Finally, the asbestos cases are uniquely result-driven, given the great public health hazard posed by asbestos. In short, *sui generis* asbestos cases are irreconcilable with the approach taken by *East River*, by the Fifth Circuit, by the Ninth Circuit, and by the great weight of maritime and common law authority.

Two subsequent Fifth Circuit decisions have reaffirmed the "object of the plaintiff's bargain" approach in maritime cases. In *Petroleum Helicopters, Inc. v. Avco Corp.*, 930 F.2d 389, 391-393 (5th Cir 1991), plaintiff bought a helicopter equipped with floats for water landings, then removed the floats and placed them on another helicopter plaintiff owned. The floats malfunctioned, causing the loss of the plaintiff's "other" helicopter that was not part of plaintiff's purchase of the floats. In defining "the product" the Fifth Circuit looked to the *nature* of plaintiff's bargain, agreeing that plaintiff "bargained for" a complete float/helicopter package and that the lost helicopter was to be considered part of "the product."[23] The court in

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[23] *See also, Exxon Shipping Company v. Pacific Resources, Inc.*, 835 F.Supp. 1195, 1201-1202 (D. Hawaii 1993) where the court

McDermott, Inc. v. Clyde Iron, 979 F.2d 1068, 1078 (5th Cir. 1992), *rev'd on other grounds*, 511 U.S. 202 (1994), also focused on the object of the plaintiff's contract to define "the product."

The other cases that have addressed this issue have uniformly held that "the product" is the finished product purchased by the plaintiffs, rather than a component part, even if that component part malfunctioned and caused the product failure.[24]

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stated: "[T]he analysis in the 'object of the bargain' test is more than a mechanical or formalistic determination of whether the injuring and injured components were sold under the umbrella of the same contract. In *Petroleum Helicopters*, they plainly were not. Instead, the court focused on the fact that the objects of the parties' bargain were the entire helicopter." The result in *Exxon Shipping* was that various components purchased separately by plaintiff under separate contracts but used as a functional unit were all considered "the product."

[24] *See, e.g., American Eagle Ins. Co. v. United Technologies Corp.*, 48 F.3d 142, 145 (airplane engine considered part of airplane "product"); *King v. Hilton-Davis*, 855 F.2d 1047, 1051-1052 (3d Cir. 1988) (sprout suppressant considered part of seed potato "product"); *American Home Assurance Co. v. Major Tool and Machine, Inc.*, 767 F.2d 446, 447-448 (8th Cir. 1985) (turbine components considered part of turbine "product"); *Exxon Shipping Co. v. Pacific Resources, Inc.*, 835 F.Supp. 1195, 1201-1202 (D. Hawaii 1993) (chaffing chain considered part of mooring system "product"); *Karshan v. Mattituck Inlet Marina & Shipyard, Inc.*, 785 F. Supp. 363, 364 n.1 (E.D.N.Y. 1992) (shore power connector part of entire vessel "product"); *ERA Helicopters, Inc. v. Bell Helicopter Textron, Inc.*, 696 F.Supp. 1096 (E.D. La. 1987) (component helicopter engine part of helicopter "product").

The Ninth Circuit below followed *East River*, its Fifth Circuit progeny, and the great weight of common law authority by examining the object of Saratoga's commercial bargain with Madruga to determine "the product":

> We are guided by the policies set forth in *East River*, where the Court stated that the focus of the product should be on the failure of the purchaser to receive the benefit of its bargain. Warranty and contract law are appropriate for this type of situation. Here, the purchaser is [*plaintiff*] Saratoga Fishing and the object of its bargain was the M/V Saratoga with the components already installed. Appx. 34a.

The "components" referenced by the Ninth Circuit were the vessel's net, skiff, speedboats, fuel, and miscellaneous electronics equipment. These are the items supplied by Madruga which "completed" the M/V Saratoga, making her functional as a tuna seiner. These items were components of the M/V Saratoga as purchased by Saratoga, and as much a part of Saratoga's bargain as the vessel's hull.

There are several important reasons to focus on the product the plaintiff bargained for and purchased rather than on the components – or as here, the partial assemblage of components originally sold to Madruga – that make up that product. First and foremost, this is the most direct and efficient means of preserving the proper role of contract law, by enforcing the industry's "expectancy" that contracts will govern the rights of commercial parties and that risk allocations voluntary undertaken will be respected.

Second, allowing a commercial plaintiff to sue an upstream component manufacturer in tort not only modifies the commercial risks to which the plaintiff agreed, but alters all of the pre-existing agreements reached in the manufacture, distribution, and sale of the product:

> Implicit in the [*economic loss rule*] is the policy judgment that in a commercial context the possibility of an inadequate recovery . . . does not justify permitting a tort recovery that will allow a purchaser to reach back up the production and distribution chain, thereby disrupting the risk allocations that have been worked out in the transactions comprising that chain.

Hininger v. Case Corp., 23 F.3d 124, 127 (5th Cir. 1994), *quoting King v. Hilton-Davis*, 855 F.2d at 1054. *See also, Bocre Leasing Corp. v. General Motors Corp., supra*, 84 N.Y.2d at 689-690, 645 N.E.2d at 1197. Along with this disruption of bargained-for risk allocation comes potentially unlimited liability to downstream users and *their* contract partners depending in some way upon the economic performance of the product. Concern over such indeterminate tort liability was expressed by this Court in *East River*, 476 U.S. at 874, and by the Ninth Circuit below. *Saratoga Fishing*, 69 F.3d at 1445, Appx. 37a. The appropriate focus must therefore be on the subject of the *plaintiff's* bargain, and not upstream to some bargain to which the plaintiff purchaser was not a party.

Third, if a component manufacturer is liable in tort for harm to any product that later incorporates the

component, the economic loss rule becomes meaningless and can seldom, if ever, be applied in practice.[25]

As the Ninth Circuit observed in this case, "Seldom does one company design and build all component parts for an integrated product such as a fishing vessel." 69 F.3d at 1446, Appx. 38a. The Court in *East River* also voiced this concern:

> Since all but the very simplest of machines have component parts, . . . a holding [permitting recovery in tort for one component damaging one or more other components] would require a finding of "property damage" in virtually every case where a product damages itself. Such a holding would eliminate the distinction between warranty and strict liability.

476 U.S. at 867, *quoting Northern Power & Engineering Corp. v. Caterpillar Tractor Co.*, 623 P.2d at 330 (Alaska 1981).

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[25] This scenario is opposite the situation at bar, where a component of the initial assemblage caused damage to later-added components that were part of the "complete package" purchased by Saratoga. Under the regime advanced by Saratoga, if the reverse were true, a manufacturer of a small component part included as part of the purchaser's bargain (but not as part of the "original sale") could be liable in tort for loss of the entire vessel, which would be viewed as "other property" in relation to the component. Potentially, under tort principles the component supplier could also be liable for all of the economic losses, including lost profits, stemming from damage to the other property. The result would be the indefinite liability and difficulty in planning business behavior. The solution is to permit only contract recovery for damage to the "object of the bargain" without creating exceptions for certain components or resale situations.

Saratoga bargained for and purchased the M/V Saratoga as a complete, integrated package. The loss of items that were part of the integrated package bought by Saratoga is simply the loss of the benefit of Saratoga's bargain. Saratoga purchased the M/V Saratoga "as is, where is," and thereby accepted the risk that the vessel would fail in whole or in part to meet Saratoga's expectations.[26] Fourteen years before the M/V Saratoga sank, Martinac, Marco and Madruga entered into commercial agreements for products which became components of the integrated package later purchased by Saratoga. Each actor allocated risk of loss for product failure in their respective agreements. Saratoga now seeks to upset that allocation. The voluntary allocations of risk by which all parties planned their business behavior should not be nullified by the fortuity of a subsequent commercial sale of the "completed package" by Madruga to Saratoga.

[26] As a prudent commercial actor, Saratoga purchased the vessel without warranty, electing instead to procure insurance against the risk of loss. Saratoga insured the entire vessel, not just the newer components, and undoubtedly Saratoga's insurer did not distinguish between what Martinac originally sold, and what Saratoga initially bought from Madruga, and what Saratoga later acquired from other sources.

D. Saratoga's assertion that the appropriate legal analysis focuses on the first § 402A "product" sold is grounded in misconstruction of the relevant cases, mischaracterization of the relevant facts, and if applied will frustrate the goal of contract-driven predictability in maritime commerce.

Initially, Saratoga misinterprets *East River* as defining "the product" (for which Saratoga concedes tort damages are unavailable) as whatever the manufacturer sold, not what the commercial purchaser bought. In support, Saratoga takes out-of-context language from *East River* regarding inapplicability of the policies underlying tort recovery "when a product injures only itself." 476 U.S. at 871. Saratoga also relies on language in *East River* suggesting there was damage only to discrete components (the turbines) manufactured by defendant Delaval, and references to this damage as being to the "product itself" without clearly indicating whether "the product" meant the component or the completed ship.[27]

In order to side-step the Court's specific attention to the charterers' bargain in sections "C" and "D" of the *East River* opinion, Saratoga asserts that in the "first part" of the opinion the Court "performed its product liability analysis to determine the identity of the product at

[27] There is some ambiguity on this point in *East River*, in that the fifth cause of action apparently claimed damage to a vessel's propulsion system, apart from the turbines themselves. The Court characterized this damage *also* as "injury to the product itself." *East River* at 867. This supports the idea that each finished vessel acquired through bareboat charter constituted "the product itself."

issue," while section "D" addressed the defendant's potential warranty liability. (Petitioner's Brief, p. 22; *Amicus* Brief of All Alaskan Seafoods, Inc., p. 12.) This construction of *East River* makes no sense because there were no warranty claims before the Court. The discussion in section "D" conveys the compelling force of the public policy choice underlying the economic loss rule, and mandates application of the rule even when the plaintiff may lack a contract remedy. 476 U.S. at 875-876.

A major flaw in Saratoga's analysis is the persistent attempt to use tort principles to interpret and apply the economic loss rule, which simply asks, "What was the object of the plaintiff's bargain?" and makes tort damages unavailable to redress loss of that bargain. This flaw is apparent from Saratoga's assertion that the Ninth Circuit erred by "misreading *East River* to import contract analysis into products liability tort law." (Petitioner's Brief, p. 12.) Saratoga has completely missed the point that the economic loss rule serves as a *contract-based* limitation on application of tort principles. The economic loss rule was designed so that strict products liability analysis would *not* apply to commercial cases.

Assuming *arguendo* the efficacy of Saratoga's tort-based approach, Saratoga has overstated both the nature of the Ninth Circuit's decision and the factual context of this case, suggesting that the Ninth Circuit's holding goes far beyond the limited commercial context of the case. Saratoga erroneously asserts that the Ninth Circuit held:

> "[T]he manufacturer's 'product' is defined for strict liability as the object that was last transferred from *any* seller to a buyer, even if the seller, as in this case, is a private person and *not* a 'seller . . . who is engaged in the business of selling such a product' as defined by the Restatement (Second) of Torts, Section 402(1)(a) [*sic*] (Petitioner's Brief, p. 5); and "The Ninth Circuit interpreted *East River* to hold that a downstream sales contract between consumers determines 'the product' . . . " (Petitioner's Brief, p. 13)

This is misleading. The Ninth Circuit was not defining "the product" for strict liability purposes, but was defining the object of Saratoga's bargain for purposes of applying the economic loss rule, and did not purport to make the economic loss rule applicable to consumer transactions. Rather, the relevant sale was between two corporate commercial entities, including a seller that bought, outfitted, operated, and resold a number of multi-million dollar tuna seining vessels, including the M/V Saratoga, at a profit.[28] (Trial Ex. "A", Trial Transcript Vol. X, pp. 72, 74; Trial Ex. "Z", Trial Transcript Vol. VII, pp. 13, 19; FL 1, Appx. 118a; Testimony, Trial Transcript Vol. X, pp. 70-73, 81:17-25.)

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[28] There is no finding in the record as to Madruga's status as a seller, *i.e.*, whether he qualified as a "402A seller," and the issue was never raised or considered previously. The Ninth Circuit noted only that the sale from Madruga to Saratoga was "commercial," and, consistent with *East River*, proceeded to determine the object of Saratoga's bargain. However, as noted *supra*, there is sufficient evidence in the record to support the idea that Madruga was "in the business" of buying and selling multi-million dollar tuna seining vessels, and made a substantial profit on his corporation's sale of the M/V Saratoga. Thus, even under Saratoga's approach "the product" would be everything that Madruga sold to Saratoga.

Consistent with its emphasis on application of *tort* principles, Saratoga argues that the object of the bargain test will abrogate "fundamental products liability principles." Saratoga's argument is illogical. The first supposed "fundamental principle" is that "only commercial sellers, *e.g.*, manufacturers and distributors, not end-users of a product can be held liable for a product's defects." (Petitioner's Brief, p. 13) The implication is that Saratoga, a mere "user," is somehow left without a remedy. This argument is somewhat disingenuous. Although Saratoga purchased the vessel without warranty coverage, Saratoga was fully insured for its loss. The sound public policy enunciated in *East River* establishes the economic loss rule applies irrespective of whether a disappointed commercial purchaser might be left without a direct remedy against the seller. 476 U.S. at 875. Saratoga also asserts that " . . . the 'product' at issue in products liability analysis is the product the manufacturer or distributor placed into the stream of commerce." (Petitioner's Brief, p. 13.) Again, application of the economic loss rule is a function of contract, not an exercise in tort, and therefore determining the "product" for strict liability purposes is irrelevant. Next, Saratoga argues "products liability cannot be disclaimed by warranty." As noted in *East River* at 476 U.S. at 873, n.8, *citing Keystone Aeronautics Corp. v. R. J. Enstrom Corp.*, 499 F.2d 146, 149 (3rd Cir. 1974), this is simply wrong. Finally, Saratoga urges that "[t]he consumer's cause of action does not depend on the validity of his contract with the person from whom he acquires the product. . . . " (Petitioner's Brief, p. 13) While this is true where strict products liability applies, a commercial purchaser cannot escape the reach of the

economic loss rule merely by suing parties further up the chain of distribution in tort, instead of suing the immediate seller solely based on contract.

Saratoga has ignored the goal underlying the economic loss rule: preservation of voluntary risk allocation between parties to a commercial contract. Preservation of the voluntary risk allocation is achieved by permitting only contract remedies for failed commercial contract expectancies. Saratoga's approach of applying tort principles to define "the product" is confusing and conflicts with the purpose of the economic loss rule by allowing tort recovery under *some* circumstances for the loss of *some* of a commercial purchaser's bargain. And sometimes, by fortuity of timing, the purchaser would recover in tort for the vast majority of its bargain, *e.g.*, if the failed component causing loss of the entire product was added just prior to the sale. Such *partial* protection of voluntary risk allocation methods is not consonant with the goals of uniformity and predictability in maritime commerce.

One case refusing to allow tort recovery in a similar situation is *King v. Hilton-Davis*, 855 F.2d 1047 (3d Cir. 1988). In *King*, Hilton-Davis was the manufacturer of a sprout suppressant used to treat seed potatoes. Hilton-Davis sold its product to defendant Kearney, who treated his seed potatoes with the sprout suppressant before selling the completed "seed potato" package to potato farmer King. Mr. King's entire potato crop failed due to ineffective sprout suppression. The Third Circuit refused to permit Mr. King's recovery in tort for the consequent loss of his potato crop:

> As we read *East River,* it is the character of the loss that determines the nature of the available remedies. When loss of the benefit of the bargain is the plaintiff's sole loss, the judgment of the Supreme Court was that the undesirable consequences of affording a tort remedy in addition to a contract-based recovery were sufficient to outweigh the limited interest of the plaintiff in having relief beyond that provided by warranty claims. The relevant bargain in this context is that struck by the plaintiff.

855 F.2d at 1051. The Third Circuit continued at 1052:

> Focusing on the Kings' bargained-for expectations, we hold that the relevant product in this case "injured only itself." The Kings contracted to buy a single integrated product, seed potatoes . . . The Kings lost the expected performance of the seed potatoes, no more and no less. (*Citing Shipco,* 825 F.2d at 928)

Like the Kings, Saratoga purchased a single integrated product: a fully outfitted tuna seining vessel. Saratoga lost the expected performance of the vessel, no more and no less.

E. Saratoga's lost catch of tuna is a consequential economic loss within the economic loss rule, and Saratoga's tort recovery for that loss should be reversed.

Direct loss of the physical object of the purchaser's bargain is the clearest example of a failed contractual expectation which is not compensable in tort. However, the economic loss rule as iterated in *East River,* and interpreted by other courts, extends to *indirect* forms of failed

expectations as well.[29] Even Saratoga concedes "warranty law . . . governs damage to the product itself or *consequential losses* . . . " (Petitioners Brief, p.10.) [*emphasis added*] The Ninth Circuit's decision, insofar as it affirmed the award of tort damages for the "lost catch," is at odds with the policies underlying the economic loss rule. By permitting tort recovery in a commercial case for a loss that is within warranty protection, a conflict between the Fifth and Ninth Circuits has arisen.

East River recognized that a warranty action allows a disappointed purchaser to "seek to recoup the benefit of its bargain," including such indirect losses as forgone business opportunities. (476 U.S. at 868, 873.) One of the factors favoring the Court's adoption of the economic loss rule was the warranty action's "built-in limitation on liability . . . from the agreement of the parties and the requirement that consequential damages, such as lost profits, be a foreseeable result of the breach." 476 U.S. at 874, *citing Hadley v. Baxendale,* 9 Exch. 341, 156 Eng. Rep.

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[29] In a case antedating *East River, Nobility Homes of Texas, Inc. v. Shivers,* 557 S.W.2d 77, 78 n.1 (Tex. 1977) the Texas Supreme Court explained economic losses can be either direct or consequential: "Direct economic loss may be said to encompass damage based on insufficient product value; thus, direct economic loss may be 'out of pocket' – the difference in value between what is given and received – or 'loss of bargain' – the difference between the value of what is received and its value as represented. Direct economic loss also may be measured by costs of replacement and repair. Consequential economic loss includes all indirect loss, such as loss of profits resulting from inability to make use of a defective product." (*quoting* Note, Economic Loss in Products Liability Jurisprudence, 66 Colum.L.Rev. 917, 918 (1966)).

145 (1854). In light of this factor, if the goal is to permit only contract recovery for expectancy losses, then "consequential damages" must fall within the economic loss rule. Otherwise, a commercial seller is exposed to the same indeterminate damages which the economic loss rule seeks to avoid. This Court previously recognized the problem, stating:

> Permitting recovery for all foreseeable claims for purely economic loss could make a manufacturer liable for vast sums. It would be difficult for a manufacturer to take into account the expectations of persons downstream who may encounter its product. In this case, for example, if the charterers – already one step removed from the transaction – were permitted to recover their economic losses, then the companies that subchartered the ships might claim their economic losses from the delays, and the charterers' customers also might claim their economic losses, and so on. "The law does not spread its protection so far." *Robins Dry Dock & Repair Co. v. Flint*, 275 U.S. 303, 309 (1927). *East River*, 476 U.S. at 874.

By excluding the consequential loss of catch from the effect of the economic loss rule, the Ninth Circuit has created the same problem of indeterminate liability discussed above, and the corresponding difficulty in planning business behavior. If Saratoga's "lost catch" is regarded as damage to "other property" compensable in tort, then, but for laches, Respondents may be liable to the tuna cannery for its lost profits and costs, and even to downstream retailers, who expected to make a profit from the M/V Saratoga's tuna catch. And courts dealing

with the economic loss claims of "downstream" commercial actors arising from damaged "other property" would have to engage in the same "murky line drawing" that the Court sought to avoid in *East River*, 476 U.S. at 875.

Other courts, including the Fifth Circuit, have given the economic loss rule the broad effect needed to fulfill its purpose of preserving contract recovery for contract losses, by applying the rule to consequential commercial losses. Instead of mechanically applying a "product itself" versus "other property" analysis, these courts, representing the clear majority view, resolve the issue with reference to the basic contract law inquiry whether the particular loss represents a commercial purchaser's failed contractual expectations. In each of the cases discussed below, the "property" which was found by the court to be "economic loss" was distinct physical property that was *not* acquired by the purchaser as part of the transaction by which the defective product was purchased (which seems to be the hallmark of the rule applied by the Ninth Circuit). In these cases, the damaged "other property" which is deemed to be economic loss was either part of an integrated system with the defective product, property which the defective product was being used to create or process in some way, or property that was naturally used or present in conjunction with the defective product. Each of these situations is analogous to Saratoga's lost fish catch. Each of these cases seems to apply the lesson that consequential contract damages of the type recoverable since *Hadley v. Baxendale, supra*, are not recoverable in tort.

The property in question was part of an integrated system with as was the defective product in *Midwhey*

Powder Co. v. Clayton Industries, 460 N.W.2d 426 (Wis.App. 1990), where the Wisconsin court found that damage to turbines used in conjunction with a defective steam generator was economic loss:

> The turbines were connected to the steam generators as an integral part of a total energy saving system. While a steam generator and a turbine may in other circumstances be sufficiently functionally distinct to be regarded as separate property, under the facts of this case when each is a component of a single system integrally connected to one another as part of an overall apparatus designed to produce electricity, the turbines cease to be separate property. 460 N.W.2d at 429.

Of course, the same logic would apply, not only to the lost tuna catch, but equally to the net, skiff, and other property not part of the original sale by Martinac to Madruga. The point is that damage to commercial property used or present in conjunction with a product that turns out to be defective quite often satisfies the requirements of *Hadley v. Baxendale, supra*, or U.C.C. § 2-715. If the seller had reason to know that his product would be used in a particular application such that its failure could foreseeably damage other property used in conjunction therewith, and the defective product proximately causes the loss, such loss is "consequential damage" recoverable under warranty.

The Minnesota Supreme Court in *Minneapolis Society of Fine Arts v. Parker-Klein Asocs. Architects, Inc.*, 354 N.W.2d 816, 819 (Minn. 1984) held that in a commercial setting, a purchaser of defective brick could not recover damages in tort for the cost of repairing and replacing a

portion of the structure into which the brick had been incorporated. Again, the damaged property was not acquired by the purchaser as part of the brick purchase, and was physically distinct from the defective brick, yet was a consequential economic loss and therefore non-recoverable in tort.

In *Palco Linings, Inc. v. Pavex, Inc.*, 755 F.Supp. 1269, 1275-1276 (M.D.Pa. 1990), the purchaser of a faulty reservoir lining sought tort damages to other parts of its construction work at the reservoir site proximately caused by the defective lining. The court, applying Pennsylvania law, held this damage to plaintiff's separate physical property to be economic loss. The analogy between the lost catch and "work in progress" is obvious. In order to make a profit, Saratoga had to use the vessel to locate, store, preserve, transport, and deliver the tuna in proper condition fit for human consumption. The loss caused by the failure to complete the vessel's intended mission is the quintessential loss of the expected performance of the product purchased by Saratoga.

In the following cases, damage to "other property" which the defective product was being used to create or process was considered economic loss. In *Thofson v. Redex Industries, Inc.*, 433 N.W.2d 901, 903-904 (Minn.App. 1988), the Minnesota Appellate Court held damage to grain caused by a defective grain dryer was economic loss not recoverable in tort, because loss of the grain was the type of damage within the contemplation of the parties to a commercial transaction. In *Purvis v. Consolidated Energy Products Co.*, 674 F.2d 217, 221-223 (4th Cir. 1982) [applying South Carolina law], a case which presaged *East River*, the court refused recovery to plaintiff under a

strict liability theory for damages to his tobacco crop caused by a defective curing barn ventilation system, because such damage was an ordinary commercial risk of product ineffectiveness. The court concluded that the remedy would lie in contract, not tort. In *Holstad v. Southwestern Porcelin, Inc.*, 421 N.W.2d 371, 375 (Minn.App. 1988), the Minnesota Appellate Court rejected tort recovery for economic loss in the form of damage to cattle feed caused by a defective feed storage system; and in *Agristor Leasing v. Guggisberg*, 617 F.Supp. 902, 908 (D.Minn. 1985), another defective animal feed storage system caused damage to feed and related lost milk production from cows. Claims for both types of damage were rejected as economic loss. Finally, in *Earl Brace & Sons v. Ciba-Geigy Corp.*, 708 F.Supp. 708, 711 (W.D.Pa. 1989) a farmer's crop was destroyed by defective herbicide purchased by the plaintiff to protect his crop from weeds. Although the defendant seller had effectively disclaimed any warranty liability, the court, applying Pennsylvania law, denied tort recovery.

Two Fifth Circuit cases are in accord with the above cases to the extent they refuse to consider separate property belonging to a plaintiff commercial product user "other property," apparently preferring instead to classify damage to cargo as economic loss. As such, these cases conflict directly with the Ninth Circuit's decision below. In *Louis Dreyfus Corp. v. 27,946 Long Tons of Corn*, 830 F.2d 1321 (5th Cir. 1987), the plaintiff charterer brought an action for damage to cargo caused by flooding as a result of a defective seawater valve. The Fifth Circuit dismissed the argument that the cargo constituted recoverable "other property" under *East River* as "meritless," 830 F.2d

1328, n.5, and reached the same conclusion a few years later in *Employers Ins. of Wausau v. Suwannee River Spa Lines, Inc.*, 866 F.2d 752, 763 n.16 (5th Cir. 1989). Although neither case provides an explanation, the result in each is perfectly consistent with the idea that because damage to cargo is something naturally to be expected when products such as a vessel or its systems fail, and because such loss is a consequential loss susceptible of warranty recovery, no tort recovery is available. The Fifth Circuit's comfort with this principle is also demonstrated in *Petroleum Helicopters, Inc. v. Avco Corp., supra*, 930 F.2d at 391-393, where defective helicopter floats caused the loss of a helicopter purchased by the plaintiff in a separate transaction. Although the lost helicopter was separate property belonging to plaintiff, and "physically distinct" from the floats, it was correctly regarded as economic loss because the loss of a helicopter was *precisely* the kind of damage one would expect from failure of the floats.

Saratoga's lost tuna catch is qualitatively no different than any of the damaged items of property which the above cases found to be economic loss. The ability to find, catch, preserve, transport, and deliver a catch of tuna was the essence of Saratoga's bargain. Certainly it was within the contemplation of Madruga, as seller, and Saratoga, as purchaser, that if the vessel failed to perform as anticipated, then Saratoga's ability to deliver and sell a catch of tuna for a profit would be defeated. Without question, loss of the catch in this case is a commercial, consequential economic loss for which tort recovery is not permitted.

Finally, it is undisputed that lost profits constitute economic loss for which no tort recovery is allowed.

Petitioner's Brief, p. 8. It is also undisputed that the District Court, for purposes of calculating damages for the lost catch, treated this loss exactly like a lost profits calculation – by utilizing the price that the cannery *would have paid* for the catch, and deducting the expenses that would have been incurred in transporting the catch to the cannery. (FD 9, Appx. 178a, 179a.) The Ninth Circuit approved of the District Court's *de facto* treatment of the lost fish catch as lost profits for purposes of calculating the damages (Appx. 36a.). Under the circumstances, the lost catch of tuna should be recognized as the equivalent of lost profits not recoverable in tort.

VI. CONCLUSION

The Ninth Circuit correctly applied the "object of the bargain" test to determine that everything part and parcel to Saratoga's purchase of the M/V Saratoga was economic loss not recoverable in tort. Saratoga purchased an integrated, full outfitted vessel, "as is" and without warranties. The risk shifting method which Saratoga elected to apply was the purchase of insurance. This bargained-for allocation of risk, and the bargained-for risk allocations of all commercial actors "upstream" from Saratoga should be left unmolested.

The "economic loss" rule applied by the "object-of-the-bargain" test serve the goal of preserving contracted-for risk allocations using the contract approach of examining the plaintiff purchaser's bargain, and declaring that bargain to be off-limits to tort recovery. Saratoga's proposed rule will not effectively protect commercial risk allocations, because it arbitrarily defines "the product"

according to tort precepts, without reference to the plaintiff purchaser's bargain. Thus, Saratoga seeks to have this Court announce a rule which involves a tort analysis to *disregard* the contractual allocation of commercial risk between commercial entities.

The Ninth Circuit erred by an incomplete application of the economic loss rule in affirming a tort recovery for the lost tuna catch. The lost catch is the equivalent of lost profits, or work in progress, and clearly represents the ultimate failure of the product in this case to fulfill its primary mission. Saratoga lost the anticipated performance of the M/V Saratoga, no more and no less. The common law cases that have considered analogous losses have correctly precluded tort recovery, as does the Fifth Circuit.

For the foregoing reasons, the Court should affirm the decision of the Ninth Circuit reversing the District Court's award of damages for loss of the net, skiff, fuel and other equipment aboard the M/V Saratoga, and reverse that portion of the decision of the Ninth Circuit which affirmed the award of consequential lost profits from the fish aboard the vessel.

Respectfully submitted,

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IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1996

SARATOGA FISHING CO.,

Petitioner,

vs.

J.M. MARTINAC & CO.; MARCO SEATTLE, INC.,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

REPLY BRIEF FOR PETITIONER

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I. RESPONDENTS INCORRECTLY ASSUME THAT THE EXISTENCE OF PRE-LOSS RISK ALLOCATION IS INCONSISTENT WITH THE APPLICATION OF ESTABLISHED TORT PRINCIPLES

Although Respondents begrudgingly acknowledge the existence of a "basis for extending tort remedy into the realm of commercial contract," they deem it incomprehensible that fostering the goals of strict products liability can rise to the level of an "overriding public policy." *See* Respondents' Brief, p. 13.

Focusing solely on the existence of pre-loss risk allocation among those in the distributive chain, Respondents characterize the rule proposed by Saratoga as a giant step backward or, in other words, a retreat from the principles espoused in *East River S.S. Corp. v. Transamerica Delaval Inc.*, 476 U.S. 858 (1986).

Respondents' position reflects a basic misunderstanding of what this Court sought to accomplish in *East River* and in doing so suggests a false choice between pre-loss risk allocation and the application of established tort principles. *East River* sought harmony between contract and tort, not the elimination of tort law. Indeed, the regime envisioned by Respondents would all but nullify strict products liability as it has developed. Clearly, this Court never intended–through its affirmation of the economic loss rule–to arm manufacturers with an impenetrable shield against public accountability for the dangers present when their defective products enter the marketplace and destroy property never sold or warranted

by those same manufacturers.

Respondents' pitch for exclusive reliance upon contractual risk allocation begs the sole question raised by this case: Should the fortuity of an intermediate sale allow manufacturers of unreasonably dangerous products to escape tort liability for damages caused by their products to property they never sold or warranted? The mere existence of pre-loss contractual risk allocation to which the Respondents were not a party does not provide a basis for such an unjustified windfall.

Saratoga does not seek an *ex post facto* transfer of purely contractual losses into the realm of tort as Respondents suggest. The rule of *Nicor Supply Ships Associates v. General Motors*, 876 F.2d 501 (5th Cir. 1989) is workable and straightforward. The economic loss limitation applies to products sold and warranted by the original manufacturer, and therefore governed by contract. Those products never sold or warranted by the manufacturer, however, were never part of "the product" and therefore are "other property" and recoverable in tort.[1/]

[1/] Respondents profess fear that American industry will somehow crumble if the Ninth Circuit's vast expansion of the economic loss rule is not given effect. They claim deep concern for a hypothetical manufacturer of an add-on part which "could have been original equipment" and which destroys a vessel because of a design defect. Respondents' Brief ¶ 14-15. Suffice to say that 1) the district court and the Ninth Circuit's original and final opinions each denied recovery for any replacement parts (*Appx. 36a*); and 2) granting tort immunity to manufacturers of unreasonably dangerous products for damage to property they never sold or warranted derogates from the most basic principles of product liability.

II. THE FIFTH CIRCUIT'S DECISIONS IN BOTH *NICOR* AND *SHIPCO* SUPPORT SARATOGA'S POSITION

Respondents contend that both *East River* and *Shipco 2295, Inc. v. Avondale Shipyards, Inc.*, 825 F.2d 925 (5th Cir. 1987) support the Ninth Circuit's decision precluding recovery for damage to equipment added to the vessel following the first sale of M/V Saratoga as well as the tuna catch destroyed in the fire. Respondents are wrong.

Respondents fail to acknowledge in any way the Fifth Circuit's more recent decision in *Nicor*. In fact, the only mention of *Nicor* is in a footnote wherein the decision is cited for a proposition which it does not support. In *Nicor* the court allowed the plaintiff to recover for damage to its "other property" in tort although at the center of the controversy was a "commercial" transaction.

Rather than citing to and/or attempting to distinguish *Nicor* or otherwise explain away its significance, Respondents choose to ignore it, discussing instead at length the *Shipco* decision which preceded *Nicor*. As discussed below, the facts of *Shipco* are readily distinguishable from the present case and support Saratoga's position.

Shipco stands for the proposition that a component part manufacturer may escape tort liability where its contribution to the product originally sold fails, damaging the other components. The *Shipco* court looked to the "object of the transaction" to define "the product" rather

than the individual component parts incorporated therein. Essentially, *Shipco* prevents an end run around the economic loss rule.

In *Shipco*, however, the transaction which the court examined was the original transaction between the end product manufacturer and the initial purchaser. *Shipco*, 825 F.2d at 928. The court's holding in *Shipco* in no way suggests that had additional equipment been added to the vessel–subsequent to the first sale–that such equipment would have been deemed part of the original bargain struck.

Unlike the situation in *Shipco*, the property for which Saratoga seeks to recover was not part of the steel hulled vessel transferred to Madruga. Because the property added by Madruga (and ultimately transferred to Saratoga) was unrelated to and independent of the original transaction with Respondents, the damage to same must be considered "other property" for which recovery in tort is allowed.

III. RESPONDENTS' ATTEMPT TO RELITIGATE THE AWARD FOR SARATOGA'S LOST CATCH OF FISH IS BEYOND THE SCOPE OF THIS COURT'S GRANT OF REVIEW AND IN ANY EVENT IS MERITLESS

Although Respondents' persistence on this issue is understandable, their attempt to reargue the award of damages for Saratoga's fish catch is beyond the scope of the Court's grant of review. As shall also be discussed,

below, (in an abundance of caution), their position is simply wrong.

At issue by this grant of review is the Ninth Circuit's reduction of Saratoga's damage award based on it's determination that "the product changed" due to the intermediate sale of the vessel. Both parties petitioned for certiorari based on the Final Opinion. Respondents' petition alone requested review of the award for the lost fish catch, and that petition is still "pending" and not at issue herein. The issue of the effect of intermediate sale is irrelevant to Respondents' liability for the fish catch, as that property was solely acquired by Saratoga after the vessel's purchase from Madruga. That issue involves no significant issue of maritime uniformity or federal law.

The content of briefs on the merits is governed by Supreme Court Rule 24 (1)(a), which does not permit a party to unilaterally "raise additional questions or change the substance of the questions already presented in those documents"[2] Respondents' attempt to relitigate an issue so clearly beyond the Court's grant of review violates Rule 24 and should not be considered.

Respondents' position is nevertheless meritless. The lost tuna catch is obviously property acquired solely by Saratoga which had enormous financial value, and which was the largest component of the district court's

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[2] The Court may at its option consider a "plain error not among the questions presented but evident from the record and otherwise within its jurisdiction to decide." Sup. Ct. R. 24 (1)(a). Respondents have not claimed, nor can they responsibly claim such error by the Ninth Circuit as to the fish catch.

damage award. Expert testimony was received on the subject from two competing experts, Lester and Peckham, each of whom assigned monetary value to the catch. *Appx., 178a-179a.* Despite that purity of record, Respondents attempt to rhetorically transmute that valuable property into "work in progress" with no economic value, or into a consequential loss unrecoverable as a mere contractual expectation.

Respondents are dramatically wrong, and no maritime case has ever supported their strained position. Their primary reliance here as in the court of appeals is on a footnote in *Louis Dreyfus Corp. v. 27,946 Long Tons of Corn*, 830 F.2d 1321, 1328 (5th Cir. 1987). Respondents incorrectly argue that case supports a claim that Saratoga's lost fish catch was a mere "commercial expectation." *Louis Dreyfus* involved a loss of cargo, which by definition is not the shipowner's property, but the property of another carried for a fee. The fee the shipowner hoped to get was indeed merely an expectation which had no value until the service he was providing was completed. In contrast, the tuna catch was Saratoga's valuable property. The *Dreyfus* court concluded that the *East River* decision had no application to the facts under consideration. *Dreyfus*, 830 F.2d at 1318 n.5. *Employers Insurance of Wausau v. Suwaneee River Spa Lines, Inc.* 866 F.2d 752 (5th Cir. 1989), also cited by Respondents, is inapplicable for the same reason.

Respondents also attempt to support their argument against the other property nature of the catch by reference to a handful of state law based agricultural product liability cases. All those cases are distinguishable as non-maritime, and have been selectively culled from the

myriad of conflicting and fact-driven state product liability decisions. The agricultural cases are also distinguishable because of the manner in which the damage occurred in those cases. As *Agristor Leasing v. Guggisberg*, 617 F. Supp. 902 (D. Minn. 1985), applying Minnesota law, explains:

> Where damage results from deterioration, internal breakage or failure to live up to expectation, recovery is allowed only on a contract or warranty theory. On the other hand, where the damage is sustained from hazardous conditions or a sudden calamitous occurrence, courts would allow recovery under a tort theory.

The *Agristor* court concluded that because the grain storage unit merely failed to perform as expected, no tort based claim was possible. In stark contrast, the destruction of M/V Saratoga cannot be termed anything less than a calamitous event. The other agricultural decisions relied upon by Respondents are inapplicable for the same reasons. *Thofson v. Redex Industries*, 433 N.W. 2d, 901 (Minn. App. 1988) (also applying Minnesota law, tort damages allowed only when damage is other than that which could ordinarily be contemplated by the parties); *Purvis v. Consolidated Energy Products Co.*, 674 F.2d 216, 233 (4th Cir. 1982) (plaintiff's evidence may have demonstrated, under South Carolina law, that the barns performed their intended task poorly, but it did not establish that they posed a safety hazard). These irrelevant state law cases were properly distinguished and

disregarded by both courts below, and have no bearing herein.

IV. CONCLUSION

Maritime products liability law prior to the Ninth Circuit's Final Opinion properly recognized the boundary between tort and contract principles elucidated by *East River*. Manufacturers are not subject to tort liability for the self-destruction of the product *they* placed into the stream of commerce. *Shipco* clarified and reinforced that boundary, defining that product as the integrated subject of the original bargain. The Ninth Circuit's Final Opinion has now disturbed the harmony envisioned by *East River*. Should the Ninth Circuit's Final Opinion be given effect, manufacturer liability for placing unreasonably dangerous products into the stream of commerce will depend upon the fortuity of an intermediate sale. Such a windfall has no relation to the original bargain between buyer and manufacturer and does not serve the goals of public safety and predictability which animate products liability law.

For these reasons, Saratoga respectfully requests that the Final Opinion of the Ninth Circuit be reversed, and that judgment for Saratoga's loss of the net, skiff, fuel and miscellaneous non-replacement property be restored.

Dated: February 3, 1997

Respectfully submitted,

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Nos. 93-56344, 93-56368, 93-56501

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1995

SARATOGA FISHING CO.,

Petitioner,

vs.

J.M. MARTINAC & CO. and MARCO SEATTLE, INC.

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

MOTION BY ALL ALASKAN SEAFOODS, INC. TO FILE *AMICUS CURIAE* BRIEF

Consent to File *Amicus Curiae* Brief Granted by Saratoga Fishing Co., and denied by Respondents

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Application for Leave to File a Brief as *Amicus Curiae*

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Respondents.

On Writ of Certiorari to the United States Court
of Appeals for the Ninth Circuit

MOTION BY ALL ALASKAN SEAFOODS, INC.
TO FILE *AMICUS CURIAE* BRIEF

Applicant, ALL ALASKAN SEAFOODS, INC. ("AAS"), moves the Court for permission to file an *amicus curiae* brief in support of Saratoga Fishing Co.'s ("Petitioner") position in the captioned matter. Petitioner has consented to AAS filing an *amicus* brief, although Respondents have refused. Accordingly, leave to file must be sought pursuant to Rule 37.2

NATURE OF APPLICANT'S INTEREST

I. AAS'S INTEREST LIES IN THE UNIFORM AND WORKABLE ADMINISTRATION OF MARITIME LAW.

Applicant has a very strong interest in the disposition of this case, since it threatens to undermine traditions of admiralty practice which have been observed in this country since it was first settled, and which have been recognized in the Constitution as well as statutes and rules of procedure enacted thereafter.

AAS is a Washington corporation, owns and/or operates numerous commercial crab fishing and commercial crab processing vessels operating in U.S. and Russian waters. AAS and affiliated companies employ roughly 250 employees, engaged in catching and processing crab, on a yearly basis. While it is by no means a "seller" engaged in the business of placing products into the stream of commerce, it has on occasion purchased second hand vessels and fishing equipment from private concerns. Likewise, in the past it has sold outdated equipment to other private concerns, equipment that, subsequent to its original acquisition, was customized to meet AAS's particular needs.

The *Saratoga*[1] decision greatly impacts not only AAS's potential liability arising out of commercial transactions, but may indeed have a direct impact on how it deals with others in the course of such transactions.

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[1] *Saratoga Fishing Co. v. Marco Seattle, Inc.*, 69 F.3d 1432 (9th Cir. 1995).

II. AAS SEEKS TO INTERVENE AS *AMICUS CURIAE* AS THE NINTH CIRCUIT'S DECISION ADVERSELY AFFECTS ADMIRALTY RULES AND THE UNIFORMITY OF ADMIRALTY LAW.

In *Merchants' National Bank of Mobile v. The Dredge Gen. G.L. Gillespie*,[2] the Fifth Circuit recognized that admiralty principals are unique. Admiralty includes concepts and procedures which are separate and distinct from the common law. These concepts and procedures date to the middle ages and have evolved over time to accommodate and meet the needs of international trade and commerce.

The *Gillespie* court recognized that:

> The Federal Courts have a great responsibility to speak consistently in maritime controversies because of their recognized national and international significance. They must take care not to fashion rules and exceptions for a particular circumstance without assessing their impact in other situations. The rules and procedures in the maritime environment must apply equally to gigantic ocean-going oil tankers traveling from the Middle East to Japan and to small inland barges . . . 663 F.2d at 1347.

The federal courts are responsible for applying admiralty law consistently and uniformly when confronted with products liability admiralty actions. The product

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[2] 663 F.2d 1338, 1346-51 (5th Cir. 1980), *cert. denied*, 456 U.S. 966 (1982).

liability rules which they fashion must apply equally to vessels which travel between circuits and those vessels which do not leave the boundaries of a single circuit. The Ninth Circuit's decision in *Saratoga* threatens the uniformity which the federal courts have sought to assure in products liability admiralty actions. The decision creates a conflict among the circuits and all but repudiates established precedent within such Circuit. The Supreme Court has accepted Saratoga Fishing's request that it carefully review the Ninth Circuit's decision in an earnest attempt to remove this conflict and clarify the holding of the Court's landmark decision in *East River*.[3]

Like the court in *Gillespie*, this Court has often recognized the need for uniformity in maritime matters.[4] Uniformity will become impossible to maintain if the circuits apply different products liability rules in the maritime products liability setting.

In order to preserve the uniform and effective administration of maritime law, this Court must reverse the

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[3] *East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858 (1986).

[4] See, for example, *Offshore Logistics, Inc. v. Tallentire*, 477 U.S. 207 (1986); *Moragne v. State Marine Lines*, 398 U.S. 375 (1970); *Kermarec v. Compagnie Generale Transatlantique*, 358 U.S. 625 (1959); *Pope & Talbot v. Hawn*, 346 U.S. 406 (1953); *London Co. v. Industrial Commission*, 279 U.S. 109 (1929); *Union Fish Co. v. Erickson*, 248 U.S. 308 (1919); *Chelentis v. Luckenback S.S. Co.*, 247 U.S. 372, 382 (1918); *Southern Pacific Co. v. Jensen*, 244 U.S. 205, 216-217 (1916); and *Lord v. Goodall*, 102 U.S. 541 (1881).

Ninth Circuit decision in *Saratoga*.

III. FOLLOWING *SARATOGA*, AND ABANDONING THE ESTABLISHED, COMMON SENSE REASONING OF THE FIFTH CIRCUIT IN *NICOR*, HAS ALREADY LED TO HORRIBLE CONSEQUENCES WHICH WILL NO DOUBT CONTINUE.

AAS, having suffered the wrath of *Saratoga* first-hand, can offer the Court a unique and separate perspective, as both a commercial processor and a consumer damaged by a defective and dangerous product, from that of *Saratoga* in the present case.

On July 24, 1994, the M/V ALL ALASKAN, a seafood processing vessel was destroyed in a tremendous fire which caused more than $100 million in property and related damages, the death of one crewman, and personal injuries of over 40 crewmen.

The vessel was purchased by AAS in the summer of 1987 and, ultimately, converted to a seafood processing vessel for use in Russian waters. In 1990, AAS installed what is commonly referred to as pipe heating cable to a section of drainage pipe in one of the vessel's cargo holds. The cable was to keep the pipes from freezing in sub-zero temperatures.

Less than a month before the fire, AAS transferred the vessel - as outfitted for seafood processing - to a joint venture ("AAS-DMP") created to handle AAS's Russian fishing operations.

AAS claims that the fire which destroyed the vessel was caused by defective heating cable which had been

installed in the vessel. The manufacturer of the heating cable, RAYCHEM CORPORATION, was not in the business of selling fishing vessels although it was well aware that its products were being used in marine applications such as that employed by AAS.

Upon RAYCHEM's Motion for Partial Summary Judgment, The Honorable Judge Barbara Jacobs Rothstein, United States District Judge for the Western District of Washington, at Seattle, dismissed the overwhelming majority of AAS's claim, based almost exclusively on *Saratoga* and the Ninth Circuit's misinterpretation of *East River*.

Judge Rothstein held - based entirely on the Ninth Circuit's analysis in *Saratoga* - that "the vessel" that internally transferred for tax purposes from AAS to AAS-DMP was "the product," including the heating cable that had been added by AAS years following the original purchase of the vessel in 1987. Under the District Court's analysis, there was no "other property" damage. [A true and correct copy of Judge Rothstein's Ruling is attached hereto and marked Exhibit "A"]. AAS is interested as *amicus curiae* in that a clarification of the strict liability principals of *Saratoga* may not encompass the issues involved in the litigation between AAS and RAYCHEM CORPORATION as decided in Judge Rothstein's ruling.

Judge Rothstein clearly followed *Saratoga*, as she was obliged to do. Her ruling - as does *Saratoga* - undermines the doctrine of strict products liability, by making AAS the purported "seller" of a defective product to itself. Had the fire occurred two weeks earlier, RAYCHEM CORPORATION would have had no defense to AAS's action.

Clearly, *East River* was never intended to shield

manufacturers from the consequences of their actions based on the "luck of the draw," i.e., a manufacturer's liability depends on whether or not it is lucky enough to have its product incorporated into another's and then resold.

AAS will concentrate only on the nature of admiralty practice, the manner in which the Ninth Circuit's decision conflicts with decisions of this Court, prior Ninth Circuit decisions, and other circuit courts of appeal, as well as upon the detriment to admiralty practice which will result if the Ninth Circuit's decision in *Saratoga* is allowed to stand.

WHEREFORE, ALL ALASKAN SEAFOODS, INC. respectfully requests that this Honorable Court, pursuant to Rule 37.2, grant its Motion to proceed *amicus curiae* in the instant action.

DATED this 27th day of November, 1996.

RESPECTFULLY SUBMITTED

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UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON
AT SEATTLE

ALL ALASKAN SEAFOODS, INC., AAS-OMP MANAGEMENT PARTNERSHIP, L.P. by KODIAK MARINE PROTEIN, INC., General Partner, Holding Company DALMOREPRODUCT, SANDRA KEGLEY, Individually, on behalf of her minor children, and as Personal Representative of the Estate of KYLE LYNN SMITH, and SHIN NIHON GLOBAL CO., LTD.,	
Plaintiffs,	NO. C96-351R
v.	ORDER GRANTING DEFENDANT RAYCHEM'S MOTION FOR PARTIAL SUMMARY JUDGMENT
RAYCHEM CORPORATION,	
Defendant and Third-Party Plaintiff,	
v.	
MARINE ELECTRIC, INC.,	
Third-Party Defendant.	
MARINE ELECTRIC, INC.,	
Fourth-Party Plaintiff,	
v.	
WESTINGHOUSE ELECTRICAL SUPPLY CO.,	
Fourth-Party Defendant.	

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WESTERN DISTRICT OF WASHINGTON AT SEATTLE
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THIS MATTER comes before the court on a motion for partial summary judgment by defendant and third party plaintiff Raychem Corporation. Having reviewed the motion together with all documents filed in support and in opposition, and being fully advised, the court finds and rules as follows:

On July 24, 1996, a fire broke out on board the P/V ALL ALASKAN, a seafood processor operating in the Bering Sea. The fire caused extensive damage to the vessel as well as the death of one crewmember and personal injury to numerous others. Plaintiffs All Alaskan Seafoods, Inc. ("AAS") and AAS-OMP Management Partnership, L.P. ("AAS-OMP") sued defendant Raychem Corporation under strict liability and negligence theories on the grounds that the fire was caused by defects in heating cable manufactured by Raychem.

Raychem now moves for partial summary judgment based on the economic loss rule adopted by the United States Supreme Court in East River S.S. Corp. v. Transamerica Delaval, Inc., 476 U.S. 858 (1986), and applied by the Ninth Circuit in Saratoga Fishing Co. v. Marco Seattle, Inc., 69 F.3d 1432 (9th Cir. 1995). The economic loss rule provides that a plaintiff cannot recover in tort for damages resulting from a product harming itself. Thus, the economic loss stemming from the damage to the product itself such as repair costs, decreased value and lost profits is not recoverable in tort. However, harm to persons and property other than the product is compensable under a tort theory.

The underlying rationale of the economic loss rule is that contract law, particularly the law of warranty, is the proper

mechanism for addressing controversies over product malfunction where the alleged damage is to the product itself. Raychem accordingly contends that plaintiffs cannot recover in tort for any property damage to the vessel itself resulting from a malfunction of an integrated vessel component like the heating cables.

Plaintiffs AAS and AAS-DMP present two types of responsive argument:

1. Legal and factual distinctions.

First, plaintiffs argue that the situation in this case is legally and factually distinguishable in several ways from those in East River and Saratoga Fishing. The court finds no basis for this argument. Saratoga Fishing is especially apposite, involving as it does a fire aboard a fishing vessel allegedly caused by a defect in the design of the hydraulic system. The Ninth Circuit concluded in Saratoga Fishing that plaintiff could not recover tort damages from the system designer for harm to the finished vessel because that was the product which plaintiff had purchased.[1]

Nor is there any basis for plaintiffs' argument that tort recovery is permitted under East River when, in addition to damaging itself, the product also causes personal injury or damage

[1]Plaintiffs contend that the court should not rely on Saratoga Fishing because it postdated the fire in this case and established new precedent which should not be applied retroactively. On the contrary, Saratoga Fishing did not announce any new legal principle, but simply applied the holding of East River to a particular fact situation.

to other property. In Saratoga Fishing, the fire not only damaged the vessel, but also other property. The Ninth Circuit carefully distinguished between the two, finding that recovery of tort damages was permissible for the latter harm, but not the former.

There is no basis in applicable caselaw for plaintiffs' argument that the gravity or catastrophic nature of the harm makes any difference to their ability to recover tort damages for harm to the product itself. As for plaintiffs' contention that the heating cable was not an integral component of the vessel because it was not necessary to the basic functioning of the vessel, the court finds that the heating cable was an integral part of the vessel within the meaning of the economic loss rule as explicated in East River and Saratoga Fishing. Nothing in the rationale of East River requires that the malfunctioning part of the product must be essential to its basic operation.

Regarding plaintiffs' failure to warn claims, they are also subject to the economic loss rule enunciated in East River. Even assuming that some exception to the rule might exist for failure to warn claims arising after the sale of a product or integral component of a product, Raychem's alleged awareness of a defect in the heating cable predated the sale and installation of the cable and the ensuing fire aboard the P/V ALL ALASKAN by many years. If plaintiffs were allowed to circumvent the economic loss rule simply by alleging a failure to warn about a pre-existing defect, the exception could well swallow the rule. East River and its progeny give no indication that this result was intended.

2. Ownership of the vessel.

Plaintiffs' other line of argument focuses on the ownership of the vessel at the time of the fire. Raychem's contention is that plaintiff AAS-DMP owned the vessel on July 24, 1994 and that AAS has no standing to bring this action because it sold the vessel to AAS-DMP effective July 5, 1994. Raychem further argues that as the purchaser of the vessel of which the heating cable was an integral component, AAS-DMP is bound by the economic loss rule set forth in East River.

Raychem bases its ownership allegations on the fact that plaintiffs recorded a bill of sale with the United States Coast Guard reflecting the transfer of the vessel's ownership from AAS to AAS-DMP on July 5, 1994. AAS-DMP also claimed ownership of the vessel when it applied for and received the insurance proceeds for losses suffered as a result of the fire. AAS-DMP further represented to the Internal Revenue Service that it was the owner of the vessel at the time of the fire and received the attendant tax benefits to be derived from that status.

AAS and AAS-DMP now seek to convince the court that AAS-DMP was not really the owner of the vessel on July 24, 1994 because there was no effective transfer of ownership until May 24, 1995 when the bill of sale was recorded with the United States Coast Guard.

The court is not persuaded. Every piece of evidence in the record including written documents by plaintiffs themselves and the actions which they took after the fire is consistent with

Raychem's contention that the transfer of ownership of F/V ALL ALASKAN took effect on July 5, 1994. The fact that the bill of sale was not recorded until much later has no bearing on when the parties reached agreement about the transfer of ownership or when that transfer was legally effective.

In a final attempt to escape the legal implications of the transfer of ownership, plaintiffs contend that even assuming the transfer took place on July 5, 1994, it had no legal meaning because AAS and AAS-DMP are, as a practical matter, one and the same entity. In essence, plaintiffs are contending that the transfer was a sham transaction from which they derived the intended financial benefits, but which should now be disregarded because it also entails some adverse legal consequences. The court refuses to be a party to plaintiffs' attempt to escape the full legal ramifications of a contract into which they freely and voluntarily entered and from which they have profited.

Defendant Raychem's motion for partial summary judgment is GRANTED.

DATED at Seattle, Washington this 7th day of June, 1996.

BARBARA JACOBS ROTHSTEIN
UNITED STATES DISTRICT JUDGE

Nos. 93-56344, 93-56368, 93-56501

IN THE
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October Term, 1995

SARATOGA FISHING CO.,

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On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF ALL ALASKAN SEAFOODS, INC., *AMICUS CURIAE*, IN SUPPORT OF SARATOGA FISHING CO.'S WRIT OF CERTIORARI GRANTED BY THE COURT ON OCTOBER 15, 1996

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Application for Leave to File a Brief as *Amicus Curiae*

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No. 93-56344, 93-56368, 93-56501

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BRIEF OF ALL ALASKAN SEAFOODS, INC., AMICUS CURIAE, IN SUPPORT OF SARATOGA FISHING CO.'S WRIT OF CERTIORARI GRANTED BY THE COURT ON OCTOBER 15, 1996

All Alaskan Seafoods, Inc. ("AAS") respectfully submits this Brief as *amicus curiae* in support of Saratoga Fishing Co.'s Writ for Certiorari which was granted by this Honorable Court on October 15, 1996.

QUESTION OF LAW PRESENTED

Whether the Ninth Circuit's approach in defining "other property" damage for purposes of invoking the "economic loss rule" undermines the Doctrine of Strict Products Liability as adopted in this Court's decision in *East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858 (1986).

I.

THE NINTH CIRCUIT'S DECISION IN *SARATOGA* IMPROPERLY DEFINES "THE PRODUCT" FOR STRICT LIABILITY PURPOSES AS THE LAST OBJECT TRANSFERRED WITHOUT TAKING INTO ACCOUNT WHAT ALLEGEDLY DEFECTIVE ARTICLE THE MANUFACTURER ACTUALLY SUPPLIED TO THE INITIAL PURCHASER

In *Saratoga Fishing Co. v. Marco Seattle, Inc.*, 69 F.3d 1432 (9th Cir. 1995), the Court of Appeals for the Ninth Circuit denied recovery to a fishing vessel owner for items of personal property which had been added by the original owner subsequent to the initial sale. Specifically, following the "first sale" by the manufacturer of the vessel (J.M Martinac & Co.) to the initial owner (Joseph Madruga), the vessel was outfitted with a seine and other fishing equipment.

Two years after the first sale of the vessel to Joseph Madruga ("Madruga"), it was purchased by Manual S. Vargas, Jr. Corporation ("second sale"), which thereafter changed its name to Saratoga Fishing Co. (hereinafter referred to collectively as "Saratoga"). The purchase price of the vessel at the time of this "second sale" included the seine, five speed boats, a skiff, electronic equipment, fuel, spare parts and other miscellaneous items which had been installed,

or otherwise placed upon the vessel following the first sale.

The Ninth Circuit, while affirming Saratoga Fishing Co.'s right to recover tort damages for its lost tuna catch, reversed the District Court's decision which allowed tort recovery for damages to property which had been placed upon the vessel as of the date title had passed to Saratoga via the second sale. According to the Court of Appeals, while the lost tuna catch amounted to "other property" - separate and distinct from that which was transferred at the time of the second sale - the remaining items for which recovery was allowed did not. *Id.* at 1445.

In so holding, the Ninth Circuit in a 2-1 opinion reasoned:

> The vessel that Martinac sold to Madruga constituted the 'product' as far as Madruga was concerned. We must decide whether the 'product' changed when Madruga added various components . . . and resold it to Saratoga Fishing.
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> Here, the purchaser is Saratoga Fishing and the object of its bargain was the M/V SARATOGA with the components already installed. Saratoga Fishing purchased the vessel 'as is.'
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> Saratoga Fishing is the second buyer in this case. We must therefore focus on its agreement with Madruga. We see no reason to extricate Saratoga Fishing from its bargain . . . The 'product' in this case is the

> vessel that was delivered to Saratoga Fishing. Because it included the skiff, net, fuel, spare parts, and miscellaneous equipment, those items are part of the product and are not recoverable in a tort action as 'other property.'

Id. at 1444 - 1445.

By focusing its inquiry on the second sale, the Ninth Circuit insulated J.M. Martinac & Co. ("Martinac") and Marco Seattle, Inc. ("Marco") from the direct and foreseeable consequences of placing an unreasonably dangerous piece of machinery, the vessel's hydraulic system, into the stream of commerce although as a result of the equipment's premature failure, personal property which neither defendant supplied sustained damage. Since the property damaged was not designed, manufactured or supplied by Martinac or Marco, it must be viewed as "other property" damage for which recovery in tort may lie.

In determining what constitutes "the product" for strict liability purposes and, thus, what is to be deemed damage other than to "the product" itself, the appropriate focus must be on the original manufacturer and its sale to the initial user. Stated in its simplest terms, only one question need be asked: "What product did the original manufacturer supply at the time the allegedly defective product was placed on the market?" Acting Justice Noonan, in his concurring and dissenting opinion, recognized the inherent fallacy of the majority's reasoning, when he noted:

> I concur in the opinion of the court, except as to its exclusion of damages for the skiff, seine net, fuel, spare parts and other miscellaneous equipment sold by Madruga to Saratoga Fishing . . . ***None of this property was manufactured or sold by Martinac*** . . . Saratoga Fishing is here the ultimate consumer; Martinac is the original seller; ***the property damaged was Saratoga Fishing's and no more a part of the product sold by Martinac than was the tuna catch for which damages are granted.***

Id. at 1447 (emphasis added).

The Ninth Circuit too - at least upon its initial consideration of the issue presented -realized that the appropriate point to begin its analysis was to determine not what had been sold to Saratoga in 1974, but instead, what had been supplied by Martinac to Joseph Madruga in 1972, at the time of the "first sale."[1]

In its original opinion, issued April 25, 1995, the Court of Appeals noted:

> We agree with the Fifth Circuit's approach. Defining the product as the object of the contract between the manufacturer and purchaser comports with the language and policy of *East River*. A product liability plaintiff is not able to recover for economic losses resulting from the loss of the vessel, but can recover damages for items added to the vessel by its

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[1] The final decision of the Ninth Circuit upon which Saratoga Fishing Co. seeks review from the Court actually represents one of three written opinions issued by the panel. The original opinion of the panel was issued on April 25, 1995. This opinion was later modified on August 4, 1995 and modified yet again on October 26, 1995. The reason for the changes are unclear.

> user. Because the *East River* court focused primarily on the role of warranty and contract law as the reason for limiting recovery of product liability damages, it is logical that when items are added to a vessel outside the scope of any warranty of contract between ***the initial purchaser and manufacturer***, they are other property.

[Appendix D to Saratoga's Petition for Writ of Certiorari, p. 107a] (emphasis added).

The Appellate Court continued:

> Marco and Martinac argue that most of the damages in this case . . . were attributable to the product itself. We disagree . . . [A]dditions to a vessel should be considered other property 'separate from the product that the manufacturer *originally* sold . . . ." . . . Although all of the . . . components were integral to the operation of the vessel, they were not part of the vessel that Martinac sold to McDruga [sic] in 1972. They were added later. Including these items as part of the 'product' would undermine the 'other property' exception . . . The items for which the district court awarded damages are inherently different from those component parts that were part of the vessel when it was delivered . . .

[Appendix D to Saratoga's Petition for Writ of Certiorari, p. 108a].

Focusing on what a manufacturer supplies at the time its goods are first placed on the market effectively establishes parameters of accountability and, at the same time, promotes the public policy concerns which gave rise to the creation of

"strict liability," mainly the protection of the downstream consuming public against unreasonably dangerous and defective products which cause injury or damage when used in an intended and foreseeable manner.[2] Viewing "the product" from the manufacturer's perspective further maintains the line of demarcation between tort and contract which the Court in *East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858 (1986) sought to achieve.[3]

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[2] See, *Greenman v. Yuba Power Products, Inc.*, 59 Cal.2d 57, 27 Cal. Rptr. 697, 377 P.2d 897 (1963) (where the court held that a manufacturer is "strictly liable" in tort when he places an article on the market, knowing it is to be used without inspection for defects, which proves to have a defect which, in turn, causes injury.)

[3] As a practical matter, contrary to the majority's opinion in *Saratoga*, focusing on the point at which the manufactured article first enters the marketplace actually promotes certainty in evaluating tort liability. Manufacturers and sellers of products will know in advance that they will remain accountable for all foreseeable consequences which result through the use of their products, as contemplated by The *Restatement (Second) of Torts*, Section 402A. The end result, however, will be that products will be safer. While the public will be better off, the liability of those in the chain of distribution will by no means be unlimited. The ever-present barriers which have always existed (e.g., statutes of limitations and repose, affirmative defenses such as unforeseeable misuse and assumption of the risk, distributor statutes which limit liability to those who actually manufacture defective products, etc.) will still exist as a means of curtailing overall responsibility.

The Fifth Circuit's approach, initially embraced but later abandoned by the Ninth Circuit, provides a straightforward and workable means by which a manufacturer's liability may be measured. The rule enunciated in *Nicor Supply Ship Assoc. v. General Motors*, 876 F.2d 501 (5th Cir. 1989), that a manufacturer is to be judged in terms of what it originally placed on the market, need not be changed, and certainly need not be set aside.

Accordingly, the Ninth Circuit should have left its original opinion of April 25, 1995 intact and, thus, maintained consistency among the Circuits.

The Ninth Circuit's decision must be reversed.

A.

The Ninth Circuit's "Change of Heart" is at Odds With the Court's Reasoning in *East River*

The Ninth Circuit in its first revised and final written opinions interpreted *East River* as mandating that "the product" for strict liability purposes be defined by the contract between Madruga and Saratoga. *Saratoga*, 69 F.3d at 1445. In the Appellate Court's view, the "object of the bargain" insofar as Saratoga was concerned was the M/V SARATOGA, a vessel sold "as is" by Madruga with the components already in place. *Id.* at 1444. Finding no reason to "extricate" Saratoga from the deal it had struck with Madruga for the sale of the vessel, the Court denied recovery in tort for those items which had been added subsequent to the "first sale." The reasoning adopted by the Ninth Circuit, however, is contrary not only with other circuits which have

had occasion to address the issue,[4] but wholly inconsistent with the approach adopted by the Court in *East River*.

Although the ultimate effect of *East River* was to differentiate between damages recoverable in tort and those recoverable in contract, the Court's analysis embraced two distinct issues of law. The first issue addressed by the Court was whether a commercial product injuring only itself was the type of harm against which public policy required manufacturers to protect. *East River*, 476 U.S. at 866. In other words, the Court's initial inquiry was to determine whether products liability applied to a case where only the product itself sustained damage. Once it determined that a tort action would not lie in such a situation, it then sought to apply its holding to the facts presented. For this purpose, the Court needed to define "the product" in order to ascertain whether or not "other property" damage was present.

In this part of the Court's analysis, i.e., in attempting to define "the product," the Court did not look at the "object"

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[4] As noted, the Ninth Circuit acknowledged in its original opinion of April 25, 1995, that the Fifth Circuit in *Nicor, supra,* held that in defining "the product" for strict liability purposes under *East River*, the focus must be on what article changed hands at the time the initial purchaser took possession of the item supplied by the original manufacturer. *See also Mays Towing Co. v. Universal Mach. Co.*, 755 F.Supp. 830, 833 (S.D. Ill. 1992) (where the district court held that, under *East River*, it was necessary to look only at what the manufacturer sold, i.e., engines which were subsequently installed within plaintiff's towboat, in order to ascertain what "the product" was for purposes of determining the existence of "other property" damage).

of the sale closest to the date the turbines failed. If they had, the "object" would have been characterized as the finished vessel, with all necessary components already installed, including the turbines. In fact, the Court completely ignored the paper trail surrounding the various transactions which preceded the loss, looking instead only to what Transamerica Deleval, Inc. - the manufacturer of the allegedly defective product - supplied and which made its way to the ultimate user, the bareboat charterer.[5]

The Court noted:

> [T]he first, second, and third counts allege that each supertanker's defectively designed turbine components damaged only the turbine itself. ***Since each turbine was supplied by Deleval*** as an integrated package . . ., each is properly regarded as a single unit.

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[5] In *East River*, there were a number of "transfers" which took place prior to the turbines failing. There were the initial contracts between Seatrain Lines, Inc.'s subsidiaries and Seatrain Shipbuilding Corp. There were the contracts between Seatrain Shipbuilding Corp. and Transamerica Deleval, Inc. There was the transfer upon completion of construction from the subsidiaries of Seatrain Lines, Inc. to a trustee. Thereafter, the vessels were transferred via bareboat charterer agreements. Presumably, there was many additional agreements between those involved in the design, construction and ultimate sale of the vessels, none of which were deemed pertinent to the Court's product liability analysis.

East River, 476 U.S. at 867. Under this analysis, the Court held:

> For the first three counts, the defective turbine components allegedly injured only the turbines themselves. Therefore, a strict products liability theory of recovery is unavailable to the charterers.

Id. at 875.

In defining "the product" for the purpose of determining whether strict liability was applicable to the charterers claims, the Court simply looked at what the manufacturer supplied. In defining "the product" as the turbines, together with all associated components, the Court did not analyze the actual contract executed by Transamerica Deleval, Inc. Likewise, the Court did not interpret the bareboat charterer agreements in order to determine from whose perspective the inquiry was to begin. Once it determined what the manufacturer had, in fact, supplied, the next step was effortless. Since there were no claims for damage to property other than what Transamerica Deleval, Inc. furnished, there was no strict liability in tort.[6]

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[6] Interestingly, the charterers made no claim for damage to any part of the vessel other than to the turbines. Presumably, under the Court's reasoning, Transamerica Deleval, Inc. would have been strictly liable in tort for such damages. Since it manufactured only the turbines, damage to additional components of the vessel, insofar as Transamerica Deleval, Inc. would be concerned, would be deemed "other property" damage.

Once it was determined that strict products liability was inapplicable, the Court went on to discuss warranty liability and the effect, if any, of certain contractual limitations of liability in favor of Transamerica Deleval, Inc. *Id.* at 875. Noting that the charterers could not have asserted warranty claims against Transamerica Deleval, Inc., the Court commented:

> In the charterers' agreements with the owners, the charterers took the ships in 'as is' condition, after inspection, and assumed full responsibility for them . . . . The contractual responsibilities thus were clearly laid out. There is no reason to extricate the parties from their bargain.

Id. The Court, therefore, looked to the bareboat charter agreements only in the context of potential warranty liability and only after it had defined "the product." The agreements were not used by the Court as a means of defining "the product" or "other property" damage.

Consistent with the above, the Ninth Circuit's adoption of *East River's* "as is" and "benefit of the bargain" language is misplaced given the fact that neither Martinac nor Marco's warranty liability is at issue. The only inquiry which the appellate court needed to make, for purposes of defining "the product," was whether the damages being claimed were for property which defendants supplied at the time the vessel was originally sold.

B.

Looking Through the Eyes of the Manufacturer in Determining Whether "other property" Damage Has Occurred Is Consistent With the Underlying Goals of Strict Liability

In *East River*, the Court rightfully recognized that:

> Products liability grew out of a public policy judgment that people need more protection from dangerous products than is afforded by the law of warranty.

Id. at 866. Consequently, in the Court's view, public policy demanded that responsibility for product defects be fixed where it would most effectively reduce the hazards to life and property inherent in such products that are released into the stream of commerce. *Id.* at 866-67.

Contract law, on the other hand, forces those in commercial relationships to honor the agreements they have made. Since contracting parties - through negotiation - may set the terms of the agreements they make, the failure of a purchaser to receive the "benefit of its bargain" may be considered at the time the agreement is reached. *Id.* at 870. While the manufacturer can restrict its liability, by disclaiming warranties or limiting the purchasers remedies, the purchaser too benefits in that, presumably, less is paid for the product. *Id.* at 873.

In *East River*, the Court sought to maintain the distinction between tort and contract. Its acceptance of the so-called "economic loss rule," however, in no way did away

with strict liability in tort. On the contrary, the Court struck a compromise whereby parties of relatively equal bargaining power would be free to allocate the risk of product defects among themselves, thereby preventing what the Court deemed "indefinite" liability on the part of product manufacturers when damage to the product alone occurs, whereas manufacturers whose defective products cause injury to a person or damage to "other property" would remain accountable for the foreseeable consequences of their actions.[7]

To remain consistent with the *East River* Court's analysis, the "economic loss rule" must be viewed in its proper context, in conjunction with the Doctrine of Strict Liability. While it no doubt attempts to keep parties to the terms of the agreements they strike the rule, likewise, reinforces the notion of strict liability by attributing blame on those who are best suited to prevent injury or damage due to dangerous and defective products, the product manufacturers. Accordingly, in determining in any given case what constitutes "the product," the underlying rationale for the imposition of strict liability must be taken into account and become part of the overall analysis. The case of *Board of*

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[7] As one commentator has noted, "In reality, the [*East River*] decision provides comfort to manufacturers seeking to minimize their responsibility for losses caused by their dangerous products." Steven R. Swanson, *The Citadel Survives a Naval Bombardment: A Policy Analysis of the Economic Loss Doctrine*, 12 Tulane Maritime Law Journal 135, 139 (1987). The author surmised further that, "Of course, litigation will be simplified because the manufacturer will always win these cases under the Supreme Court's holding." *Id.* at n. 22.

Education of the City of Chicago v. A, C and S, Inc., 131 Ill.2d 428, 546 N.E.2d 580 (1989) is highly instructive.

There, certain school districts brought suit against an array of entities who had supplied asbestos containing materials (ACMs) which were, in turn, incorporated into the construction of city schools. The materials at issue included acoustic tile, plaster, insulation and fireproofing material. The school districts alleged that asbestos particles had been released into the atmosphere and, as a result, had contaminated the schools.

The defendants moved to dismiss the actions based, *inter alia*, on the "economic loss rule," arguing that the plaintiffs had failed to sufficiently allege "other property" damage so as to properly fall within the realm of a tort claim. *Id.* at 585. The trial court granted the motions and on appeal the dismissals of the tort claims were affirmed. On appeal to the Supreme Court of Illinois, the dismissals were reversed, the court holding that the plaintiffs had properly alleged "other property" damage. The Supreme Court of Illinois reasoned:

> In regard to the strict liability count, the trial ruled that the ACMs were components and indivisible parts of the building and as such were not a product for strict liability purposes. An item will be considered a product for purposes of the cause of action if to do so will effectuate the policy basis for imposing strict liability in tort . . . . The fact that these [ACMs] are used in the construction and have been installed in a building does not detract from their nature as products separate from the actual structure. We cannot accept the defendants' argument that these ACM's have become permanent fixtures upon real property,

> indistinguishable from the buildings themselves, and to do so would defeat the underlying policy reasons for imposing tort or recovery.

Id. at 591. The lesson to be gleaned is that the "economic loss rule" cannot be viewed in isolation. Its application must coincide with the interests of those which the Doctrine of Strict Liability seeks to protect. Defining "the product" through the eyes of the manufacturer who first places the allegedly defective product on the market promotes the policies of strict liability and, at the same time, provides a workable means whereby exposure may be assessed by those in the chain of distribution. As noted by one commentator:

> . . . [T]he manufacturer is able to predict what damages might arise from the use of his product:
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> > The manufacturer knows the purpose for which its product is to be used and by whom. Although all purchasers are not identical, the manufacturer can determine within a reasonable range of predictability the ramifications of a product failure . . .
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> Steven R. Swanson, *The Citadel Survives a Naval Bombardment: A Policy Analysis of the Economic Loss Doctrine*, 12 Tulane Maritime Law Journal 135, 157-158 (1987).

Regardless of whether a downstream sale of an allegedly defective product occurs subsequent to the "first sale," the manufacturer must remain accountable for what it has placed on the market. The fact that the product may change hands at various times through the course of its useful life is irrelevant in terms of defining what "the product" is.

In the case of *T.H.S. Northstar Ltd. Partnership v. W.R. Grace & Co.*, 767 F.Supp. 969 (D. Minn. 1991), another asbestos case, the plaintiff purchased a downtown office building which it later learned was contaminated with asbestos containing materials. The building was purchased in 1986. Although the asbestos had been installed as part of the building's original construction and, thus, transferred by the prior owner to the plaintiff at the time title passed, the court - relying on *East River* -found "other property" damage, i.e., damage to the facility from the release of asbestos fibers, so as to justify recovery in tort.

The fact that a sale between private parties occurred subsequent to time the asbestos had originally been installed was a non-issue. Rejecting the defendants' assertion that the claim was precluded by the "economic loss rule," the district court simply looked to what the asbestos manufactures had supplied and whether or not damage to property, other than product furnished, had occurred. *Id.* at 972-974; *See also Lavwma v. Northwest Pipe & Casing Co.*, 915 F.Supp. 1066, 1071 (N.D. Cal. 1995) (where the district court, although rejecting plaintiff's claims of strict liability arising out of the delamination of a coal tar enamel lined pipe manufactured by defendants for use in plaintiff's wastewater export pipeline, noted that recovery would have been allowed had the defect complained of damaged. ". . . any separate property, such as a valve or other component of the pipeline . . . outside of the pipe itself."); *Northridge Co. v. W.R. Grace & Co.*, 162 Wis.2d 918, 471 N.W.2d 179 (1991) (where the court, finding "other property" damage under the *East River* analysis, permitted a strict liability action where defendant manufacturers supplied asbestos containing materials to a general contractor who, in turn, incorporated same into the facility it had furnished to the plaintiff); *City of Manchester v. Nat'l Gypsum Co.*, 637 F.Supp. 646 (D.R.I. 1986) (where

in a pre - *East River* decision-the court found asbestos released into the atmosphere had caused "other property" damage so as to preclude application of the "economic loss rule"); *International Knights of Wine, Inc. v. Nave Pierson Winery, Inc.*, 110 Cal. App.3d 1001, 168 Ca. Rptr. 301, 304 (1980) (where Justice Fleming, in his concurring and dissenting opinion, noted that the reasoning of *Seely v. White Motor Co.*, 63 Cal.2d 9, 45 Cal. Rptr. 17 (1965) - which was embraced by the Court in *East River* - would allow recovery against manufacturers of defective bottle caps which damaged wine contained in bottles upon which the caps were placed, the wine insofar as the bottle cap manufacturers were concerned amounting to "other property" damage and not "economic loss"); *Sacramento Regional Transit Dist. v. Flxible*, 158 Cal. App.3d 289, 204 Cal. Rptr. 736, 741 (1984) (where the court characterized the damage alleged in *International Knights, supra,* as properly alleging physical injury to plaintiff's wine caused by the defective caps plaintiff had purchased); *Kodiak Elec. Ass'n, Inc. v. Deleval Turbine, Inc.*, 694 P.2d 150, 152-54 (Alaska 1984) (where the court affirmed the imposition of strict liability where defective turbines incorporated into a diesel generator which failed and damaged an unrelated component of plaintiff's electrical power generation system, a component which the defendant did not supply, leaving in tact the trial court's finding of "other property" damage); *Hamilton Fixture Co. v. Anderson,* 285 So.2d 744 (Miss. 1973) (where the court upheld the giving of an instruction on strict liability where the manufacturer incorporated an allegedly defective humidifier as part of the central heating and cooling system installed in a new home, although the defendant had sold a "finished product" to parties who, in turn, had sold the house

which sustained damage to plaintiffs); *Fordyce Concrete, Inc. v. Mack Trucks, Inc.*, 535 F.Supp. 118 (D.Kan. 1982) (where the court upheld imposition of strict products liability a against manufacturer of a defective truck chassis which damaged a concrete mixer assembly affixed thereafter, finding same to be "other property," since the mixer assembly which sustained damage was not the item which the defendant manufacturer had supplied).

II.

THE NINTH CIRCUIT'S ANALYSIS IMPROPERLY DETERMINES A MANUFACTURER'S STRICT LIABILITY FOR A DEFECTIVE PRODUCT ON AN UNRELATED ACT OF A THIRD PARTY WHICH PLAYED NO ROLE WHATSOEVER IN PLACING THE PRODUCT ON THE MARKET IN THE FIRST INSTANCE.

The Ninth Circuit in *Saratoga* ignored the teachings of *East River* by defining Martinac and Marco's liability solely in terms of what Madruga, a private consumer, transferred to Saratoga Fishing. Madruga, however, was not a "seller" engaged in the business of selling vessels or component parts thereof. To set the parameters of a manufacturer's liability in tort based on the act of a non-seller, which plays no role whatsoever in placing a defective product on the market, is not only illogical but undermines the doctrine of strict liability as embodied in Section 402A of

the *Restatement (Second) of Torts*[8] and accepted by the Court in *East River*.

Accepting the Ninth Circuit's reasoning places Madruga, a commercial consumer, in the shoes of Martinac and Marco, the manufacturers of the allegedly defective hydraulic system, for purposes of determining what the defendants' "product" entailed. This is improper.

Section 402A of the *Restatement (Second) of Torts* applies as a general rule to "sellers" engaged in the business of selling allegedly defective products.[9] Consistent with the Court's analysis in *East River*, therefore, the limit of a manufacturer's liability is predicated on a determination of

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[8] The *Saratoga* Court approach further conflicts with established prior decisions of the Ninth Circuit wherein Section 402A was adopted as the law of the Ninth Circuit relating to products liability. *See Pan-Alaska Fisheries v. Marine Constr. & Design Co.*, 565 F.2d 1129 (9th Cir. 1977).

[9] This requirement is by no means a novel concept. It has long been held that strict liability applies only to those in the chain of distribution or, in other words, engaged in the business of selling products. *See Kealoha v. Du Pont De Nemours & Co.*, 82 F.3d 894 (9th Cir. 1996); *Muniz v. Ransomes America Corp.*, 921 F.Supp. 438, 442 (S.D. Tex. 1995) (for strict liability purposes, the defendant must have not only "supplied" the product but also must be engaged in the business of placing such products into the stream of commerce); *Bukowski v. Geo. A. Hormel & Co.*, 157 F.R.D. 50 (S.D. Iowa 1994) (strict liability not applicable to a one time seller of a piece of machinery); *Green, III v. Whiteco Industries, Inc.*, 17 F.3d 199, (7th Cir. 1994) (same).

what the manufacturer initially placed on the market, or stated another way, sold to the original purchaser. *East River*, 476 U.S. at 867; *Nicor Supply*, 876 F.2d at 506. A "seller" under Section 402A is unequivocally not a consumer such as Madruga reselling a used product to another consumer such as Saratoga Fishing.

Since Madruga was not "engaged in the business" of selling vessels, the object which he passed on to Saratoga Fishing at the time of the "second sale" cannot, and should not, serve to shape the liability of Martinac and Marco, the original product manufacturers.

A.

The Downstream Transfer of an Allegedly Defective Product Cannot Serve to Remanufacture "the Product" Which Was Originally Marketed

The Ninth Circuit, in essence, held that Madruga - by outfitting the vessel prior to its transfer to Saratoga Fishing - remanufactured "the product" which Martinac and Marco originally sold. The absurdity of allowing a subsequent act, unrelated to the initial design, manufacture and distribution of the product, to dictate ultimate responsibility for the losses sustained by Saratoga Fishing may be illustrated by two simple analogies to situations which arise in the civil litigation context each day.

The first example concerns the attorney-client privilege. It is common knowledge that, once a professional relationship is created for the purpose of obtaining legal advice, all communications, whether oral or written, between attorney and client are deemed "privileged" and, thus, protected from disclosure. The privilege, however, is not

absolute. In order to determine whether or not protection from disclosure will be afforded, the substance of, together with the facts and circumstances surrounding, the communication must be evaluated. With this in mind, it a generally accepted proposition of law that:

> [A] party cannot conceal a fact merely by revealing it to his lawyer, nor may he secrete a pre-existing document merely by giving it to his attorney.

State Ex. Rel. Dudek v. Circuit Court for Milwaukee County, 34 Wis.2d 559, 581, 150 N.W.2d 387 (1967). In other words, the act of communicating with one's attorney cannot by any means convert non-privileged information into a protected communication. Stated another way, an independent, subsequent act cannot change the overall character of the communication that originally took place.

Similarly, all involved in litigation have grappled with the ever-present "hearsay rule" of exclusion and the plethora of exceptions which have been carved out along the way. Of significance to this discussion is what is referred to as the "business record exception." As a general proposition, a document kept by a litigant in the ordinary course of business will be shielded from the preclusive effect of the "hearsay rule." Where, however, one simply places a document generated by another in his file, the exception will not apply since the document, although kept by the party seeking its introduction, was not prepared by such party. *See, e.g., Phillips v. United States*, 356 F.2d 297, 307 (9th Cir. 1965). Thus, the act of placing another's document in one's file, an act wholly unrelated to the preparation of the document itself, does not create a "business record" for purposes of applying the exception to the "hearsay rule."

The two examples cited above illustrate, quite clearly, the shortcomings of the Ninth Circuit's approach. By focusing on the subsequent, unrelated act of Madruga in transferring title of the vessel to Saratoga Fishing, the *Saratoga* Court allowed the acts of an independent, third-party (a non-seller, a non-manufacturer, a private consumer), acts which occurred long after the product was first sold, to completely alter the character of the product which Martinac and Marco placed on the market. In the Ninth Circuit's view, "the vessel" which was originally supplied was transformed via the "second sale" (a one time sale by a private concern, to another private concern), into a fully outfitted fishing vessel, complete with a skiff, seine net, processing equipment and the like. Although the item which Martinac and Marco initially supplied had, in actuality, remained the same, the liability exposure which previously existed vanished.[10]

Just as one cannot convert a non-privileged document into a protected communication by turning it over to his attorney, and cannot create a "business record" out of a

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[10] Ironically, the Ninth Circuit deemed "the sale" of the vessel to Saratoga the crucial event upon which liability would arise or disappear. What is ironic about the appellate court's approach, i.e., looking to the last sale of the item as opposed to the item which the manufactures placed on the market, is that imposition of strict liability does not require that "a sale" in the technical sense actually take place. *See Anderson v. Olmsted Utility Equipment, Inc.*, 60 Ohio St. 3d 124, 573 N.E.2d 626 (1991). If strict liability is not dependent on "a sale," it would seem improper to deem such "a sale" the mechanism for determining if accountability is justified or not.

document prepared by another, a private consumer transferring title to a previously manufactured item cannot remanufacture a product.

B.

A Manufacturer's Ultimate Liability for Product Defects Should Not Depend on the "Luck" of the Draw

In *Seely, supra.*, the appellate court recognized that:

> The distinction . . . between tort recovery for physical injuries and warranty recovery for economic loss is not arbitrary and does not rest on the 'luck' of one plaintiff in having an accident causing physical injury . . . .

Seely, 63 Cal.2d at 18, 403 P.2d at 151. The court's observation is well taken and applies equally to the present case. Simply stated, a manufacturer's liability for damages resulting from defective products should not depend on the "luck" of the manufacturer that its product or component will be sold to another (one other than the original purchaser) prior to injury or damage being caused.

Martinac and Marco should not be permitted to escape liability simply because Madruga (the original purchaser) just so happened to transfer the vessel to Saratoga Fishing. Had the transfer not taken place as of the date of the hydraulic failure, neither Martinac nor Marco would be protected, although the same product defect would be responsible for the same damages sustained.

Products liability arose out of a public policy concern that consumers needed added protection from dangerous and

defective products than existed under the law of warranty. Martinac and Marco's liability (or any product manufacturer for that matter) for precisely the same damage, caused by precisely the same product defect, should not turn on whether, by pure "luck," its product happens to be sold before the defective condition manifests.

The case of *Rosenau v. City of New Brunswick, N.J.*, 51 N.J. 130, 238 A.2d 169 (1968), a pre-*East River* decision, supports the rejection of the Ninth Circuit's approach. There, the City of New Brunswick purchased sixty (60) water meters from Worthington Gamon Meter Company of Newark ("Worthington") for incorporation into its municipal water system. The City installed one of the newly acquired meters in the home of plaintiffs. Years later, the meter in plaintiffs' home broke, causing damage to the premises.

After suit was filed, the plaintiffs' strict liability action was dismissed upon Worthington's motion for summary judgment. Plaintiffs sought certification for review by the Supreme Court of New Jersey - which was granted.

Addressing whether or not the plaintiffs were entitled to proceed in strict liability against Worthington (the manufacturer of the allegedly defective product), the Supreme Court of New Jersey commented:

> The Appellate Division's opinion seems to stress the fact that Worthington sold the meter to the City and never intended that the meter would be sold to the public . . . . But it knew that the meter would be incorporated by the City into its water supply system and that members of the public would come in contact with it when it was placed in their home. It also knew that if the meter was manufactured

> defectively . . . serious harm to persons and property would probably result.

Id. at 175. The New Jersey Supreme Court determined that plaintiffs were entitled to proceed under a strict products liability theory of recovery and remanded the case. In so holding, the court reasoned:

> The Appellant Division was apparently persuaded by the hardship which may result to Worthington by the plaintiffs pursuit grounded on strict liability in tort . . .
>
> * * *
>
> [A]lthough the plaintiffs will be relieved of the responsibility of affirmatively establishing failure to exercise due care in the process of manufacture, they will still have the burden . . . of establishing that the meter was actually defective . . .
>
> * * *
>
> On the other hand, the hardship to the plaintiffs under the Appellate Division's approach would indeed be severe . . . In considering the relevant hardships we must not lose sight of the crucial fact that Worthington originally placed the allegedly defective product in the stream of trade. As manufacturer and distributer it is the one best situated to protect against consequential damage as a business risk of distribution whereas the injured parties are wholly innocent and largely incapable of protecting themselves.

Id. at 176.

The wisdom of *Rosenau* court's discussion is readily apparent. Although the decision was not mentioned in *East River*, the reasoning ultimately adopted by the Court mirrored that of the New Jersey Supreme Court espoused nearly twenty years before. The New Jersey Supreme Court, like the Court in *East River*, ignored the fact that - prior to the incident giving rise to the claim - the allegedly defective product had changed hands. Both courts looked simply to what the manufacturer had placed on the market. In *Rosenau*, it was of no consequence that the product furnished by Worthington had been incorporated into the City's water supply system and then resold to the plaintiffs.

III.

CONCLUSION

The Ninth Circuit's decision turns the Court's analysis in *East River* on its head, creating inconsistency among the Circuits, inconsistency which will severely impact land-based and marine products liability actions alike.

The *Saratoga* decision treats private consumers as product manufacturers and sellers and manufacturers of defective products as innocent bystanders.

If *Saratoga* is allowed to stand, the clear distinction between tort and contract will eventually disappear. The "other property" exception will cease to exist since, each time a product is sold or modified, the manufacturer's liability for what it originally placed on the market diminishes.

Practicality, predictability and public policy mandates that *Saratoga* be reversed and that approval be given to the

straightforward and workable interpretation set forth by the Fifth Circuit in *Nicor*.

DATED this 27th day of November, 1996.

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(6)

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In The

Supreme Court of the United States

October Term, 1996

SARATOGA FISHING CO.,

Petitioner,

vs.

J.M. MARTINAC & CO. and MARCO SEATTLE, INC.,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF AMICUS CURIAE OF NATIONAL ASSOCIATION OF MANUFACTURERS AND RAYCHEM CORPORATION IN SUPPORT OF RESPONDENTS

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STATEMENT OF INTEREST

• The National Association of Manufacturers

The National Association of Manufacturers (the "NAM") is the nation's oldest and largest broad-based industrial trade association. Its more than 14,000 member companies and subsidiaries, including 10,000 small manufacturers, employ approximately eighty-five percent of all manufacturing workers and produce over eighty percent of the nation's manufactured goods. More than 158,000 additional businesses are affiliated with the NAM through its Associations council and National Industrial Council.

• Raychem Corporation

Raychem Corporation is a technology based manufacturing company located in Menlo Park, California. Raychem is the defendant in the case entitled *All Alaskan Seafoods, et al. v. Raychem Corporation, W. D. Wash., case no. C 95-351R,* in which a vessel owner seeks economic damages associated with the loss of its vessel, the PV/ ALL ALASKAN, when it burned. Raychem manufactures heating cable products that are wrapped around pipes and covered with insulation to keep the pipes from freezing. Its heating cable product was installed on P/V ALL ALASKAN during a conversion of the vessel into a fish processor, and is alleged to have caused the fire. One of its opponents in this lawsuit, All Alaskan Seafoods, Inc., has filed an amicus brief supporting the arguments of Petitioner.

SUMMARY OF ARGUMENT

The Ninth Circuit's approach in defining the "product," for purposes of the economic loss rule, as the "object" of the plaintiff's bargain finds its support in the fundamental premises of this Court's *East River* decision and the decisions of virtually every court to address the issue. The "object" or "benefit" of the bargain approach is the only principled way to differentiate economic losses, as that term is used in *East River*, from tortious injuries. The Ninth Circuit's rule is fair and accounts for the ability of parties to commercial transactions to allocate the risk of economic losses among them. The Ninth Circuit's decision protects the ability of upstream commercial manufacturers to make meaningful contracts limiting or disclaiming their liability, and to avoid exposure to unlimited economic losses in tort. The rules of law proposed by the Petitioner ignore the rationale of *East River* and would unravel the agreements regarding risk allocations throughout the supply chain. None of the proposed definitions of "product" are reconciled with *East River's* conclusion that tort principles are weak when a product fails or harms itself. The proposed definitions of "product" are arbitrary and incapable of application across a broad range of circumstances in any principled way. In some circumstances, the proposed definitions abrogate the economic loss rule altogether.

ARGUMENT

I. THE NINTH CIRCUIT PROPERLY APPLIED THE "BENEFIT OF THE BARGAIN" ANALYSIS SET FORTH IN THIS COURT'S OPINION IN *EAST RIVER*.

The task before the Ninth Circuit in *Saratoga Fishing Co. v. Marco Seattle, Inc.*, 69 F.3d 1432 (9th Cir. 1995), was

to determine whether the economic loss rule adopted by this Court in *East River S.S. Corp. v. Transamerica Delaval*, 476 U.S. 858 (1986) applies to the product purchased by the plaintiff, or to an earlier configuration of the product consisting of important components manufactured and supplied by the defendants. Following what is referred to in the case law alternatively as the "benefit of the bargain" rule and the "object of the bargain" test, the Ninth Circuit found that the economic loss rule precluded any claim of Saratoga Fishing Co. – plaintiff below and Petitioner here – in tort for the tuna-seining vessel that Petitioner had purchased, including the seine, skiff, electronic equipment, speed boats, fuel, spare parts and other miscellaneous items that had all been supplied to Petitioner as part of the tuna seiner. Petitioner ("Saratoga")[1] and All Alaskan Seafoods, Inc. ("All Alaskan") challenge the Ninth Circuit's use of the "benefit of the bargain" test.

In *East River*, this Court explained that "[d]amage to a product itself is most naturally understood as a warranty claim," 476 U.S. at 872, because the purchaser has failed to receive the benefit of its bargain. When a product injures itself, it fails to perform according to expectations and the purchaser does not receive the anticipated value from the product purchased. "Such damage means simply that the product has not met the customer's expectations, or, in other words, that the customer has received 'insufficient product value.' . . . The maintenance

[1] As Saratoga is the successor in interest to Manuel Vargas, who purchased the vessel from Joseph Madruga, for ease of reference "Saratoga" or "Petitioner" will always be used.

of product value and quality is precisely the purpose of express and implied warranties." *Id., quoting* J. White and R. Summers, Uniform Commercial Code 406 (2d ed. 1980). The plaintiff should avail itself therefore of contracts or warranties to recover its economic losses. "Obviously, damage to a product itself has certain attributes of a products-liability claim. But the injury suffered – the failure of the product to function properly – is the essence of a warranty action, through which a contracting party can seek to recoup *the benefit of its bargain." Id.* at 867-68 (emphasis added).

The focus in *East River* thus was on the bargain that the plaintiff, as the contracting party, had made and the fact that the plaintiff did not receive the benefits from the product it purchased. "[W]arranty law sufficiently protects *the purchaser* by allowing it to obtain *the benefit of its bargain*. . . . The expectation damages available in warranty for purely economic loss give *a plaintiff the full benefit of its bargain* by compensating for forgone business opportunities." *Id.* at 873 (emphasis added). "Even when the harm to the product itself occurs through an abrupt, accident-like event, the resulting loss due to repair costs, decreased value, and lost profits is *essentially the failure of the purchaser to receive the benefit of its bargain – traditionally the concern of contract law." Id.* at 870 (emphasis added).

The reasoning in *East River* consequently requires a court to look at what the plaintiff's actual bargain was and the product that the plaintiff purchased for purposes of defining the "product" involved. If contract and warranty law apply because the injury suffered by the plaintiff is the failure of the "product" to meet the plaintiff's

expectations, then "the product" – that part of the plaintiff's property that is governed by contract rather than tort law – can only be defined as the product that plaintiff purchased. A plaintiff negotiates warranties against product failure and appropriate price adjustments with respect to the product that it purchases, *not* with respect to a component, product, or version of the product that a former purchaser bought upstream. A previous transaction involving a product that differs from the product the plaintiff in fact bought is irrelevant.

The Ninth Circuit's opinion in *Saratoga Fishing* flows directly from *East River*. In reaching its holding, the Ninth Circuit stated, "We are guided by the policies set forth in *East River*, where the Court stated that the focus of the product should be on the failure of the purchaser to receive the benefit of its bargain. Warranty and contract law are appropriate for this type of situation. Here, the purchaser is Saratoga *and the object of its bargain was the M/V SARATOGA with the components already installed." Saratoga Fishing*, 69 F.3d at 1444 (emphasis added). The Ninth Circuit accordingly held: "The 'product' in this case is the vessel that was delivered to Saratoga Fishing. Because it included the skiff, net, fuel, spare parts, and miscellaneous equipment, those items are part of the product and are not recoverable in a tort action as 'other property.' " *Id.* at 1445. This analysis and result closely follow the reasoning and policies of *East River*.

II. THE RULE FOLLOWED BY THE NINTH CIRCUIT IN *SARATOGA FISHING* IS THE SAME RULE ADOPTED BY VIRTUALLY EVERY COURT THAT HAS CONSIDERED THE ISSUE.

Petitioner and All Alaskan contend that the Ninth Circuit's opinion in *Saratoga Fishing* conflicts with the approach taken by the Fifth Circuit. The opposite is true. The Ninth Circuit's opinion is directly derived from the Fifth Circuit's application of the "object of the bargain" analysis. There is a wealth of carefully reasoned case law adopting *East River's* focus on the plaintiff's bargain as the starting point for defining "product" under the economic loss rule. The doctrinal and commercial certainty that has developed under *East River* will be undermined if the Court were to adopt any of the several rules proposed by the Petitioner or All Alaskan.

A. *Saratoga Fishing* Is Identical To The Fifth Circuit's Approach In Cases Such As *Shipco 2295* And *Nicor*.

The seminal Fifth Circuit case is *Shipco 2295, Inc. v. Avondale Shipyards, Inc.*, 825 F.2d 925 (5th Cir. 1987). The Fifth Circuit held that components of a vessel could not be considered "other property" in language strikingly similar to that of the Ninth Circuit's *Saratoga Fishing*:

> In attempting to identify the product, our analysis leads us to ask *what is the object of the contract or bargain that governs the rights of the parties*? The completed vessels were obviously the objects of the contract. [Plaintiff] Shipco did not bargain separately for individual components of each vessel. *We are persuaded that those same vessels that were the object of the contract must be considered 'the product' rather than the individual components that make up the vessels.*

825 F.2d at 928 (footnote omitted) (emphasis added). The Fifth Circuit stated further, "The product in this context means the finished product *bargained for by the buyer* rather than components furnished by a supplier," and "The critical fact that Shipco *bargained for a finished vessel* remains unchanged." *Id.* at 929-30 (emphasis added). The court also observed that its approach is derived from *East River*: "East River teaches that such economic loss for damage *to the product bargained for*, the vessels in this case, cannot be recovered in tort." *Id.* at 929 (emphasis added).

The Fifth Circuit's subsequent opinion in *Nicor Supply Ships Ass'n v. General Motors Corp.*, 876 F.2d 501 (5th Cir. 1989), follows *Shipco 2295*'s "object of the bargain" test and is also entirely consistent with the Ninth Circuit's approach. *Nicor* held that plaintiff could not recover for fire damage to a vessel allegedly caused by a faulty fuel injector and fuel-conditioning system in a main engine. 876 F.2d at 502, 505. It also held that recovery *could* be had for equipment placed on board the vessel by a third party *after* the plaintiff's purchase of the vessel, because such equipment was *not* a part of the plaintiff's bargain. 876 F.2d at 505. The Ninth Circuit thus correctly observed that *Nicor* is not in conflict with its holding in *Saratoga Fishing*:

> In [*Nicor*], the vessel was sold only once. The buyer then time-chartered the vessel to a third-

> party, who installed equipment on the vessel. The court properly focused on the bargain between the buyer and shipbuilder to determine what was the product. . . . The equipment was deemed 'other property.'

Saratoga Fishing, 69 F.3d at 1444.[2]

B. *Saratoga Fishing*'s Application Of The "Object Of The Bargain" Test Is Also Consistent With The Practice In The Other Federal Circuits And The State Courts.

The "object of the plaintiff's bargain" test has been universally adopted. Federal and state courts agree that in determining whether a product has injured only itself or has injured "other property" for purposes of the economic loss rule, the "product" at issue is the integrated product the plaintiff purchased. The Eleventh Circuit has stated the rule concisely and in no uncertain terms: "The

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[2] Other Fifth Circuit cases are to the same effect. In *Petroleum Helicopters, Inc. v. Avco Corp.*, 930 F.2d 389 (5th Cir. 1991), a helicopter was damaged when an emergency floatation device (originally sold to plaintiff with another helicopter) allegedly malfunctioned during a water landing and caused the helicopter to capsize. The Fifth Circuit held that damage to the helicopter constituted economic loss and could not be recovered under a product liability theory against the manufacturer of the float. 930 F.2d at 393. In *American Eagle Ins. Co. v. United Technologies Corp.*, 48 F.3d 142, 145 (5th Cir. 1995) *modified on other grounds on reh'g*, 51 F.3d 468 (5th Cir. 1995), the defendant sold a defective engine to Cessna Caravan Aircraft, which installed it in an aircraft. The aircraft was sold *five times*, the last purchaser being plaintiff Martinaire, Inc. The Fifth Circuit expressly focused on the object of plaintiff Martinaire's bargain, and held that the "product" was the aircraft that Martinaire purchased.

character of loss determines the appropriate remedies, and, to determine the character of a loss, *one must look to the product purchased by the plaintiff, not the product sold by the defendant." Pulte Home Corp. v. Osmose Wood Preserving, Inc.*, 60 F.3d 734, 741 (11th Cir. 1995) (emphasis added) (*quoting Casa Clara Condominium Ass'n v. Charley Toppino & Sons, Inc.*, 620 So. 2d 1244, 1247 (Fla. 1993)). The Third Circuit agrees:

> As we read East River, it is the character of the plaintiff's loss that determines the nature of the available remedies. When loss of the benefit of a bargain is the plaintiff's sole loss, the judgment of the Supreme Court was that the undesirable consequences of affording a tort remedy in addition to a contract-based recovery were sufficient to outweigh the limited interest of the plaintiff in having relief beyond that provided by warranty claims. The relevant bargain in this context is that struck by the plaintiff. It is that bargain that determines his or her economic loss and whether he or she has been injured beyond that loss."

King v. Hilton-Davis, 855 F.2d 1047, 1051 (3d Cir. 1988), *cert. denied*, 488 U.S. 1030 (1989). The overwhelming number of federal and state courts that have considered the issue of what constitutes "the product" for purposes of *East River* have employed the "object of the bargain" test and held that "the product" is the product purchased by the plaintiff.[3]

---

[3] *See, e.g., Hininger v. Case Corp.*, 23 F.3d 124 (5th Cir. 1994); *American Home Assurance Co. v. Major Tool & Mach., Inc.*, 767 F.2d 446, 447-48 (8th Cir. 1985); *Bowling Green Mun. Utils. v.*

The Petitioner and All Alaskan invite the Court to disregard this body of authority in favor of decisions that predate or fail to follow *East River*. None of the cases cited by Petitioner or All Alaskan announce a rule that supports their arguments, or provide any guidance to the Court in fashioning a rule that would not severely restrict the import of *East River*.[4]

Thomasson Lumber Co., 902 F. Supp. 134, 139 (W.D. Ky. 1995); *Exxon Shipping Co. v. Pacific Resources, Inc.*, 835 F. Supp. 1195, 1200-01 (D. Haw. 1993); *Karshan v. Mattituck Inlet Marina & Shipyard Inc.*, 785 F. Supp. 363, 364 n.1 (E.D.N.Y. 1992); *ERA Helicopters, Inc. v. Bell Helicopter Textron, Inc.*, 696 F. Supp. 1096 (E.D. La. 1987); *Bocre Leasing Corp. v. General Motors Corp.*, 84 N.Y.2d 685, 645 N.E.2d 1195 (1995); *Casa Clara Condominium Ass'n v. Charley Toppino & Sons, Inc.*, 620 So. 2d at 1247; *Utah Int'l, Inc. v. Caterpillar Tractor Co.*, 108 N.M. 539, 541-42, 775 P.2d 741, 743-44 (Ct. App.), *cert. denied*, 108 N.M. 354, 772 P.2d 884 (1989).

[4] In some of these cases, as *Nicor* held, the courts merely upheld products liability claims for damage to property or equipment that the plaintiff (subsequent to purchase) added to, combined or used with the "product." *See, e.g., McDermott, Inc. v. Clyde Iron*, 979 F.2d 1068 (5th Cir. 1992) (defective crane purchased by plaintiff and deck being moved by crane both damaged; tort recovery allowed for damage to deck but not to crane); *Mays Towing Co. v. Universal Mach. Co.*, 755 F. Supp. 830 (S.D. Ill. 1990) (plaintiff purchased defective engines and installed them in its river towboat; plaintiff was not able to recover in tort for damage to engines, but could recover for damage to the rest of the vessel). In other cases, the courts' conclusions were controlled by the very state law approaches rejected by *East River*. *See Rosenau v. City of New Brunswick, N.J.*, 51 N.J. 130, 238 A.2d 169 (1968) (permitting recovery for damage to the product itself); *Sacramento Regional Transit Dist. v. Flexible*, 158 Cal. App. 3d 289, 205 Cal. Rptr. 736 (1984) (same); *Kodiak Elec. Ass'n v. Delaval Turbine, Inc.*, 694 P.2d 150, 153-54 (Alaska 1984) (same); *Fordyce Concrete, Inc. v. Mack Trucks, Inc.*, 535 F. Supp. 118, 124-25 (D. Kan. 1982) (same). The remaining cases – those involving asbestos contamination of public buildings and shopping centers – do not counsel abandoning the "object of the bargain" approach. These cases turn on the unique nature both of the "defect" of asbestos and the damage it causes. *See, e.g., Board of Educ. of the City of Chicago v. A, C and S, Inc.*, 131 Ill. 2d 428, 446, 546 N.E.2d 580, 588 (1989). They hold that asbestos actions are a hybrid of economic loss, personal injury, and physical damage to property. *See City of Manchester v. National Gypsum Co.*, 637 F. Supp. 646, 649-50 (D.R.I. 1986); *Northridge Co. v. W.R. Grace & Co.*, 162 Wis.2d 918, 932, 471 N.W.2d 179, 184 (1991); *A, C and S, Inc.*, 546 N.E.2d at 588. These cases accordingly find that the harm suffered by the plaintiffs does not fit within the usual definition of "economic loss" because breakdown of asbestos causes dispersion of a "hazardous," "dangerous" and "highly toxic substance" that is injurious to the occupants and to the public that uses the buildings. *See T.H.S. Northstar Ltd. v. W.R. Grace & Co.*, 767 F. Supp. 969, 973-74 (D. Minn. 1991); *City of Manchester*, 637 F. Supp. at 650-51; *Northridge Co.*, 471 N.W.2d at 184, 186; *A, C and S, Inc.*, 546 N.E.2d at 588, 590.

III. THE "OBJECT OF THE BARGAIN" TEST APPLIED BY THE NINTH CIRCUIT IS FAIR BECAUSE IT PRESERVES THE TERMS OF THE PLAINTIFF'S BARGAIN AND HONORS THE CONTRACTUAL ARRANGEMENTS MADE IN UPSTREAM TRANSACTIONS.

A. It Is Fair To Leave Petitioner To The Terms Of Its Bargain.

Commercial parties to a sale can and are expected to negotiate price and to allocate their respective rights, risks, liabilities, and remedies. A purchaser may obtain extensive warranties and pay more for a product, or it may decide to forego warranties, accept (and perhaps insure) the risk that the product might malfunction, and

obtain a discounted price. Petitioner thus is not left unprotected by the Ninth Circuit's unwillingness to extend tort remedies to some of the vessel's components. Instead, at the time it struck its bargain with Madruga, Petitioner had every opportunity, through warranty or insurance, to protect itself from economic disappointment if the fully outfitted purse seiner failed to perform.

The fairness of holding commercial parties to their bargains is one of the fundamental premises of *East River*. "Contract law, and the law of warranty in particular, is well suited to commercial controversies of the sort involved in this case because the parties may set the terms of their own agreements. The manufacturer can restrict its liability, within limits, by disclaiming warranties or limiting remedies. . . . In exchange, the purchaser pays less for the product. Since a commercial situation generally does not involve large disparities in bargaining power, . . . we see no reason to intrude in the parties' allocation of the risk." 476 U.S. at 872-73. The Court accordingly stated that "[t]here is no reason to extricate the parties from their bargain." *Id.* at 875.[5]

[5] Courts applying the economic loss rule have made similar observations. The Eleventh Circuit in *Pulte Home Corp.* stated: "The rationale underlying the economic loss rule is that parties should protect against the risk of economic loss during contract negotiations through warranty provisions and price adjustments rather than attempt to recovery under tort law after the loss occurs." 60 F.3d at 739-40. *See also Detroit Edison Co. v. Nabco, Inc.*, 35 F.3d 236, 240 (6th Cir. 1994): "The rationale behind this definition of economic loss is that losses based on damage to the product itself are the sort of losses that can and should be addressed by the parties in negotiating the conditions and specifications of a sale.

By defining "the product" to include the components Madruga added to transform the P/V Saratoga into an operational tuna seiner, the Ninth Circuit kept Petitioner to the terms of its bargain as *East River* requires. Any definition of "the product" that looks to an earlier sale would "extricate" commercial parties from their bargains. If a plaintiff can reach upstream and sue a manufacturer in products liability when the product it purchased fails, that plaintiff receives not only the benefit of the lower price it negotiated but also a supplement to its reasonable economic expectations in the form of products liability remedies against a manufacturer. Because it is reasonable to hold commercial parties to their bargains, however, courts have focused on the *plaintiff's* bargain and have refused to permit this "supplement." *See, e.g., Pulte Home Corp.*, 60 F.3d at 742 ("Having failed to avail itself of the opportunity to mitigate the risks of potential disappointment at the time of contract negotiation, [plaintiff] cannot now resort to the courts to save it from a bargain improvidently made").

B. The "Object Of The Bargain" Test Protects The Contractual Arrangements That Had Been Negotiated Upstream From Plaintiff's Bargain.

The commercial realities observed by the Supreme Court in *East River* also apply in upstream transactions during production of the product purchased by the plaintiff. Manufacturers selling components to be used in complex products such as a tuna seiner make contracts with

each other, third parties, and purchasers with regard to the risks and liabilities associated with fabricating the completed product. In each instance, such manufacturers set their price, and have the opportunity to negotiate warranties and impose limitations on their liability for the economic consequences if their components fail.

Contractual arrangements that limit liability for property damage and related losses – either in tort or warranty – are valid in a commercial context.[6] It is perfectly natural for a supplier, presumably in exchange for a lower profit, to disclaim liability for losses that may arise in a commercial endeavor. The economic loss rule respects these upstream transactions by permitting only contract and warranty remedies in commercial controversies that arise when products fail to operate properly.

Although valid between suppliers and buyers of components to be used in ultimate products, and between sellers and buyers of finished products, liability limitations are difficult to impose on remote purchasers.[7] Tort liability may be even more difficult to contain effectively

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[6] *East River*, 476 U.S. at 873 n.8 (citing *Keystone Aeronautics Corp. v. R.J. Enstrom Corp.*, 499 F.2d 146, 149 (3d Cir. 1974)); *Agip Petroleum Co. v. Gulf Island Fabrication, Inc.*, 920 F. Supp. 1330, 1341 (S.D. Tex. 1996) ("Under admiralty law, clauses limiting liability for negligence and strict liability are valid and enforceable." [citing *Nicor*]) This also is the rule in land-based cases. *See, e.g., McDermott*, 979 F.2d at 1076; *Idaho Power Co. v. Westinghouse Elec. Corp.*, 596 F.2d 924 (9th Cir. 1979).

[7] *Hininger*, 23 F.3d at 124, *citing Patty Precision Products Co. v. Brown & Sharpe Mfg Co.*, 846 F.2d 1247, 1257 (10th Cir. 1988) ("it may be difficult or even impossible for a component manufacturer to disclaim its warranty liability") .

with contractual arrangements. *King*, 855 F.2d at 1050. Were it not for the economic loss rule, these difficulties in limiting liability to downstream purchasers would expose component suppliers to uncertain and far-reaching liability. Because contractual limitations of liability are difficult to impose except on direct purchasers, any resale of a component – even before it was integrated into a finished product – would transform a commercial relationship with fixed allocation of risks and remedies into an inquiry about public duties, product defect and limitless economic consequences. *See East River*, 476 U.S. at 874.

The plaintiff's bargain is the appropriate place to start in defining the "product" because, that is the transaction where the plaintiff has an opportunity to fix its own economic expectations regarding the product it is purchasing. Defining the product on the basis of any upstream transaction (such as Madruga's purchase of some parts of the tuna seiner) carries with it the likelihood of nullifying the commercial arrangements of upstream participants in the supply chain. If the "product" does not change as new components are added to it, or it is modified, the economic loss rule loses touch with the plaintiffs' bargain and exposes suppliers to liability for downstream commercial expectations, however they may have tried to control their liability when selling their products or components.[8]

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[8] *See Bocre Leasing Corp.*, 84 N.Y.2d at 693, 645 N.E.2d at 1199, a thoughtful decision by the New York Court of Appeal explaining its adoption of the economic loss rule and its focus on the plaintiff's bargain.

"Given the reality of already existing, ample deterrents to manufacturers injecting unsafe products into the commerce

Courts, accordingly, have refused invitations to define "products" on the basis of upstream transactions. *King*, 855 F.2d at 1054 ("Implicit in the [economic loss rule] is the policy judgment that in a commercial context the possibility of an inadequate recovery . . . does not justify permitting a tort recovery that will allow a purchaser to reach back up the production and distribution chain, thereby disrupting the risk allocations that have been worked out in the transactions comprising that chain"); *Hininger*, 23 F.3d at 127; (same). *Saratoga Fishing*, by ruling that the "product" was defined by the plaintiff's bargain merely adopted the reasoning of these courts, extracted directly from *East River*, that it was

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stream, and the resultant lack of a substantive public policy purpose to be furthered by imposing additional tort liability in these circumstances, no tort recovery can be had against the manufacturer for contractually based economic loss, whether due to injury to the product itself or consequential losses flowing therefrom. . . .

Tort recovery in strict products liability and negligence against a manufacturer should not be available to a downstream purchaser where the claimed losses flow from damage to the property that is the subject of the contract. Transforming manufacturers into insurers, with the empty promise that they can guarantee perpetual and total public safety, by making them liable in tort for all commercial setbacks and adversities is not prudent or sound tort public policy. In such instances, no directly related or commensurate public interest is served or protected by holding manufacturers liable. Tort law should not be bent so far out of its traditional progressive path and discipline by allowing tort lawsuits where the claims at issue are, fundamentally and in all relevant respects, essentially contractual, product-failure controversies. Tort law is not the answer for this kind of loss of commercial bargain."

unfair to disrupt an entire chain of commercial arrangements in order to augment the plaintiffs' available remedies for its own commercial disappointment.[9]

In recognition of the same values that yielded the *East River* decision, the Court should affirm the Ninth Circuit's application of the "object of the bargain" test. It differentiates between the "product" and "other property" in a way that conforms to commercial expectations and protects the ability of all parties to strike meaningful bargains. There is no reason to prefer – and, in fact, every reason to subordinate – the plaintiff's ability to recover in tort to the attempts by upstream suppliers to control their liability. After all, the plaintiff had an opportunity at the time of purchase to protect against economic disappointment.

C. The Ninth Circuit's Benefit Of The Bargain Approach "maintain[s] a realistic limitation on damages."

This Court declared in *East River* that in addition to keeping products liability and contract law in separate

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[9] Petitioners and All Alaskan complain that the Ninth Circuit's application of the "object of the bargain" test is unfair because recovery for the components added to the vessel by Madruga then depends on "bad luck" that the product failed after it was purchased. First, plaintiff's recovery depends not on luck, but on how it has chosen to arrange its commercial risks when striking its bargain. Second, the "bad luck" is far more likely to fall on the suppliers of components. If Petitioner's views were adopted, such suppliers' attempts to control liability through contractual arrangements will be scuttled by fortuitous resale of their products to a remote purchaser with whom they have no contract or opportunity to negotiate.

spheres, it adopted the economic loss rule out of a concern "to maintain a realistic limitations on damages." 476 U.S. at 871. The Court observed, "A warranty action also has a built-in limitation on liability, whereas a tort action could subject the manufacturer to damages of an indefinite amount." *Id.* at 874. It explained further:

> In products-liability law, where there is a duty to the public generally, foreseeability is an inadequate brake. . . . Permitting recovery for all foreseeable claims for purely economic loss could make a manufacturer liable for vast sums. *It would be difficult for a manufacturer to take into account the expectations of persons downstream who may encounter its product.* In this case, for example, if the charterers – *already one step removed from the transaction* – were permitted to recover their economic losses, then the companies that subchartered the ships might claim their economic losses from the delays, and the charterers' customers might also claim their economic losses, and so on. 'The law does not spread its protection so far.' "

Id. (citations omitted).

Petitioner's and All Alaskan's proposal that the first sale of a product by the manufacturer determine the "product" for all transactions downstream disregards the concern for putting a limit on damages downstream. Their approach subjects manufacturers to liability for all alterations to, modifications or updating of, or repairs to the product by all purchasers subsequent to the original sale. If products are used in the "modification" of a vessel, Petitioner and All Alaskan would make the manufacturer, even of the most trivial component, liable for all

lost profits associated with the use of the "original" product. The Ninth Circuit's ruling in *Saratoga Fishing* and implements this Court's directive to avoid such limitless economic exposures.

IV. PETITIONER AND ALL ALASKAN FAIL TO PROPOSE A RULE FOR DECISION THAT SQUARES WITH *EAST RIVER*.

Petitioner and All Alaskan suggest that the Ninth Circuit should have applied any number of "rules" which would make tort remedies available against these defendants. What undermines all of their approaches is that *East River* already has reconciled the restriction of tort remedies with the advantages of applying contract law to economic losses. Petitioner's and All Alaskan's artificial attempts to segregate *East River's* discussion of contract law from its products liability analysis reflects a fundamental misunderstanding of the decision – a misunderstanding that is at the heart of every challenge they make to the Ninth Circuit's ruling.[10]

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[10] Petitioner and All Alaskan claim that *East River* contains two separate and independent discussions, the first an analysis of products liability law, followed by a discussion of warranty laws. Petitioner's brief at 19-24; All Alaskan's brief at 9-12. This Court knows best what it intended, but it appears quite plain from the opinion and it certainly has been the reaction of the judiciary that *East River* defined economic losses from the perspective of the plaintiff's bargain. The decision simultaneously considered tort and contract law, and determined that warranty law more appropriately addressed the failure of a product to meet a plaintiff's expectations – or, as the Court put it, "the failure of the purchaser to receive the benefit of its bargain," 476 U.S. at 870.

A. Arguments That A Product Is Any Physically Distinct Article That A Seller Places In Commerce Ignore The Premises Of *East River*.

Petitioner and All Alaskan analyze the issue of what constitutes "the product" exclusively from the point of view of the manufacturer of the defective product rather than of the bargain struck by the plaintiff. They insist again and again that "the product" must be defined by the defective product the manufacturer has placed on the market. *See* Petitioner's brief ("Pet. Br.") at 3-4 ("the product in products liability cases, including maritime products liability cases, is determined by what the *manufacturer* places in the stream of commerce"); All Alaskan's brief ("All Al. Br.") at 4 ("the appropriate focus must be on the *original manufacturer* and its sale to the *initial user*") and 16 ("the product" must be defined "through the eyes of the manufacturer") (emphasis added) *See also* Pet. Br. at 8, 9, 12, 18, 24, 27, 29, 34-35; All Al. Br. at 2, 7 n.3, 13, 20-21.[11]

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[11] As support for these broad statements, Petitioner and All Alaskan offer a single remark in the *East River* opinion supposedly showing that the manufacturer's sale rather than the plaintiff's bargain was the focus of the Court's concern. Because the Court observed that "[s]ince each turbine was supplied by Delaval as an integrated package, . . . each is properly regarded as a single unit," 476 U.S. at 867, Petitioner and All Alaskan claim that this Court was asserting a rule that "the product" must be defined as that product "supplied by the manufacturer." *See, e.g.*, Pet. Br. at 21; All Al. Br. at 10-11. The Court's comment that each turbine was properly regarded as a single unit was offered in the context of the Court's *rejection* of the theory that one component could damage another. *See* 476 U.S. at 867. The Court was not addressing the issue of whether any other component *of the vessels* might or might not be considered part of the product. Because no other component of the vessels was harmed, the Court did not have to discuss that issue.

Petitioner struggles a bit itself with the breadth of its argument when it acknowledges that – under both *Shipco 2295* and *Nicor* – harm to any or all components of a vessel which is the object of the plaintiff's bargain is immune to a tort theory. Pet. Br. at 29-30. To avoid application of this rule here, Petitioner argues that the "skiff, net, fuel, spare parts, speed boats and miscellaneous equipment added to M/V SARATOGA . . . are physically distinct individual products in their own right. . . . " *Id.* at 31. This characterization of the equipment, however, fails to advance the discussion at all. A fully outfitted tuna seiner is as capable of being called a "physically distinct product in its own right" as a partially outfitted vessel. Surely the vessels in *Nicor* and *Shipco 2295* employed components that might be called physically distinct. Yet the courts in those cases analyzed the "product" in terms of the plaintiff's bargain, not by when "physically distinct" elements were added to the vessel.

Petitioner and All Alaskan also argue that, unless the product is defined by the manufacturer's sale of the article, the public policy of strict products liability will be compromised. They suggest that holding a manufacturer accountable in tort will "establish parameters of accountability," will protect the downstream consuming public, will attribute "blame on those who are best suited to

prevent injury or damage due to dangerous and defective products, the product manufacturers," and that the "end result . . . will be that products will be safer." *See* Pet. Br. at 17-19; All Al. Br. at 14. Again, these considerations were part of the Court's calculus in *East River*. The Court determined that these tort law policies were weak and warranty law was primary when a product purchased by the plaintiff damages itself and causes economic loss. 476 U.S. at 871. It makes no sense, then, to turn to tort policies when determining how "the product" should be defined.

Finally, Petitioner and All Alaskan vigorously argue that the stability of maritime law is threatened by the benefit of the bargain analysis applied by the Ninth Circuit. The court's analysis, however, already has stood the test of many maritime and land-based judicial decisions and offers an objective, fair and certain measurement of "the product" that conforms to accepted commercial realities. The approach offered by Petitioner and All Alaskan, to the contrary, is arbitrary and impossible to implement. Although it is clear that Petitioner would prefer to measure the product from the Martinac/Madruga transaction in this case[12], it is wholly unclear how a future case

[12] *See* Pet. Br. at 12-13. Petitioner suggests that Madruga was the "first" or "original" buyer. This is circular reasoning. For example, if the "product" were the hydraulic system that malfunctioned aboard the M/V SARATOGA, Martinac – who purchased it from Marco – would be the "first" buyer. Conversely, if the product is the fully outfitted purse seiner, Madruga – who purchased all of the components and assembled them to his specifications – would be the first buyer. In other words, unless the product already has been defined, it is impossible to identify the "first buyer."

would be resolved. It is difficult to imagine how courts will distinguish between components and products when the rule proposed calls for entire ships to be the "product" on the one hand, but – with only the fact that they must have been sold by a manufacturer as guidance – for partially outfitted tuna seiners to be the "product" on the other.[13]

B. The "Static" Product Argument Ignores Commercial Realities And The Premises Of *East River*.

Petitioner argues that the Ninth Circuit erred by asking whether the product "changed" when Madruga completed outfitting of the vessel. Pet. Br. at 22-23. All Alaskan, similarly argues that a downstream purchaser cannot "remanufacture" a product placed on the market by an initial manufacturer. All Al. Br. at 21-24. Both argue that, since Madruga added components to the vessel *after* his bargain with Martinac, Respondents would have been liable in tort for this "other property" but for the "fortuity" or "pure luck" of a resale to Saratoga. Pet. Br. at 32-33; All Al. Br. at 23-25. Both claim the Ninth Circuit

[13] It is even more difficult to conceive how All Alaskan would have this Court distinguish between a manufacturer's "components" and its "products." The item at issue in its case with Raychem – an electrical heating cable – is a small, inexpensive wiring product that was physically integrated into the vessel. Any workable rule of law that purports to implement *East River*, *Shipco 2295*, and *Nicor* must account for the differences between such components of the vessel and the vessel itself.

decision thus poses a problem of "vanishing" tort liability. *Id.*

There are at least three defects in this reasoning. First, a resale (particularly of a significantly changed product) is not a fortuitous or chance event. It is a commercial transaction in which the purchaser has the opportunity to control its economic risks. Petitioner concedes that it is common for vessels to be outfitted for a particular purpose and resold. Pet. Br. at 9-10. Just using the facts of the *Saratoga Fishing* and *All Alaskan v. Raychem* as examples, in both cases the owner/user of the vessel made substantial, commercial changes to the vessels. In *Saratoga Fishing*, Madruga contracted with other vendors after he took title to the vessel to complete outfitting it for tuna fishing, always its intended purpose. In *All Alaskan v. Raychem*, the seller of the vessel contracted with a shipyard to convert its vessel (once a military vessel) to a salmon processor. Both of these sellers added components, large and small, to the vessel with the help of experienced shipyards and suppliers. When the buyers of those vessels bargained for them, they had already been outfitted for their intended purposes. It makes little sense and certainly depends on fortuity to say that the very modifications to the vessel that make it what it is are not part of the product because they happened to occur after a fishing company took title to the vessel.

Second, *East River* already makes it plain that tort liability may change as components and products change hands. By definition, if the economic loss rule has any vitality, it must protect component manufacturers from tort liability for losses arising if the component damages

the ultimate product.[14] Before the component is integrated into the product and sold, however, the manufacturer may well have – absent a contractual disclaimer – a tort remedy if the component damages other property.[15] After the component is integrated into the product and sold, however, *East River* has already determined that there is no tort recovery available for harm to the (new) product itself from the manufacturer *or* the component manufacturer.

Last, the products liability that Petitioner and All Alaskan posit has "vanished" may well not exist in the first place. Because the supplier may have contracted to limit its tort liability with the "original" buyer, tort liability – if the Ninth Circuit's approach is rejected – may "spring" into being rather than "back to zero" upon a resale. The fact is that Petitioner and All Alaskan are talking about two very different activities when they compare potential tort liability to Madruga for the equipment he added versus potential tort liability to Saratoga for loss of the purse seiner. In the first, Martinac and Marco had an opportunity to allocate risks among themselves and Madruga including for equipment he added to

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[14] In *East River*, quoting *Northern Power & Eng'g Corp. v. Caterpillar Tractor Co.*, 623 P.2d 324, 330 (Alaska 1981), the Court observed, " 'Since all but the very simplest of machines have component parts, [a contrary] holding would require a finding of 'property damage' in virtually every case where a product damages itself. Such a holding would eliminate the distinction between warranty and strict liability.' " 476 U.S. at 867.

[15] This is essentially the holding in *Nicor* where "other property" added to that which formed the plaintiff's bargain was recoverable in tort.

the vessel. In the second, Saratoga Fishing had every opportunity to protect against economic losses caused by the performance of the product it purchased, the fully outfitted purse seiner. *East River* makes it clear that it is appropriate to treat these transactions differently.

C. Whether Or Not A Seller Is A "Restatement Section 402A Seller" Is Irrelevant To This Court's Analysis In *East River*.

Petitioner has proposed one more test to determine "the product" that is found in neither *East River* nor the case law concerning the economic loss rule. According to Petitioner, "the product" is that which is sold by a seller who fits within section 402A of the Restatement (Second) or Torts. Pet. Br. at 28. Conversely, Petitioner proposes that a transaction involving a non-402A seller cannot be the transaction that determines what "the product" is, even if it is the transaction in which the plaintiff made its purchase. *Id.* at 28. In keeping with its proposed "test," Petitioner goes to great lengths to argue that Madruga, the person who sold the seining vessel to Petitioner, was "a consumer" and an "occasional seller," and was not a 402A seller. *Id.* at 13, 14, 16. *See also* All Al. Br. at 19-21.[16]

Section 402A, however, is entirely irrelevant to this Court's analysis in *East River*. There is no discussion

[16] In making this argument, Petitioner improperly draws factual conclusions about Madruga's status as a 402A seller on the basis of issues that were never litigated before the District Court and of "facts" that were never the subject of any findings by the Court.

concerning and no determination made whether any of the sellers, owners, or charterers involved are 402A sellers. Indeed, *there is no meaningful discussion of section 402A in all of East River*. Section 402A is only mentioned twice in passing, once parenthetically to indicate that one of the Courts of Appeals adopted section 402A in applying strict liability law in admiralty, and once to observe *that section 402A does not answer the question before the Court*. 476 U.S. at 865, 868 n.3. In addition, *no other court following East River or applying the economic loss rule has analyzed or even mentioned whether a 402A seller was involved in the sale of the "product" subject to the economic loss rule.*[17] Section 402A by its express terms does not address the issue presented to the Ninth Circuit in *Saratoga Fishing*. It contains the following caveat: "The Institute expresses no opinion as to whether the rules stated in this Section may not apply . . . to the seller of a component part of a product to be assembled."

[17] *American Eagle Ins.*, in particular, establishes that a seller's status under § 402A has nothing to do with the definition of "the producer." After Cessna purchased and installed the engine in an aircraft, it sold the aircraft to Federal Express Corporation, which presumably does not engage in the business of selling aircraft as required by § 402A(1)(a). *See American Eagle Ins.*, 48 F.3d at 143-44. The aircraft was then sold *four more times* after Federal Express purchased it. The Fifth Circuit, however, did not analyze whether any of the aircraft's purchasers were § 402A sellers. Rather, the Fifth Circuit focused solely on the aircraft as the object of the bargain of *plaintiff*, the fifth and last purchaser.

Under Petitioner's proposed rule, the economic loss rule simply "vanishes" with respect to any components that happen to be installed and integrated into products by "occasional" sellers. Madruga, if he were found to be an occasional seller, would not be liable in strict liability for the hull *or* the equipment he added. His status therefore, does not contribute anything to Petitioner's argument that damage to some components of the purse seiner are governed by tort law while other losses are recoverable only in contract. Section 402A, after all, is intended to determine *who* is responsible if there is any products liability, not *whether* there is liability in the first place. Petitioner's proposed "test" based on a seller's status under § 402A is irrational and must be rejected.

V. CONCLUSION

The Ninth Circuit applied the rationale of *East River* to reach a fair result that is consonant with the approach taken by every Federal court to consider the issue. The National Association of Manufacturers and Raychem Corporation respectfully urge the Court to affirm the Ninth Circuit's ruling with regard to the equipment added by

Madruga to fully outfit the M/V SARATOGA before it was sold to Petitioner for tuna fishing.

Respectfully submitted,

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